

Education Achievement Authority

**Financial Report
with Supplemental Information
June 30, 2016**

Education Achievement Authority

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Independent Auditor's Report

To the Board of Directors
Education Achievement Authority

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the major fund, and the aggregate remaining fund information of the Education Achievement Authority (the "School District", the "Authority", or the "EAA"), as of and for the year ended June 30, 2016, and the related notes to the financial statements, which collectively comprise the Education Achievement Authority's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the major fund, and the aggregate remaining fund information of the Education Achievement Authority as of June 30, 2016 and the respective changes in its financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

To the Board of Directors
Education Achievement Authority

Emphasis of Matter

The accompanying basic financial statements have been prepared assuming that the Education Achievement Authority will continue as a going concern. As discussed in Note 1 to the basic financial statements, the Authority was created through an interlocal agreement with Eastern Michigan University and Detroit Public Schools. The interlocal agreement allows for one of the parties to withdraw from the agreement. In the event that the party withdraws from the agreement and another entity does not take its place, the Authority would no longer have a legal basis for operating. Eastern Michigan University has indicated they will not renew the interlocal agreement and no other organization has taken its place. As such, the Authority will cease to operate and exist at June 30, 2017. At this date, the Authority will cease leasing the buildings and operating. All facilities will return to the Detroit Public Schools Community District.

As described in Note 13 to the basic financial statements, the Authority incurred certain expenditures under grant programs that may be disallowed and recovered upon review of the granting agency, resulting in potentially material changes to federal source revenue recognized.

As discussed in Note 13 to the basic financial statements, the Education Achievement Authority is a defendant in a number of litigation matters that have occurred during the course of operations. Our opinion is not modified with respect to this matter.

The basic financial statements do not include any adjustments that might result from the outcomes of these uncertainties.

Required Supplemental Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and the major fund budgetary comparison schedule, as identified in the table of contents, 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, which 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 supplemental 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.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated November 14, 2016 on our consideration of the Education Achievement Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Education Achievement Authority's internal control over financial reporting and compliance.



November 14, 2016

Education Achievement Authority

Management's Discussion and Analysis

This section of the Education Achievement Authority's (the "EAA," the "Authority," or the "School District") annual financial report presents our discussion and analysis of the EAA's financial performance during the year ended June 30, 2016. Please read it in conjunction with the EAA's financial statements, which immediately follow this section.

Using this Annual Report

This annual report consists of a series of financial statements and notes to those statements. These statements are organized so the reader can understand the EAA financially, as a whole. The government-wide financial statements provide information about the activities of the whole district, presenting both an aggregate view of the EAA's finances and a longer-term view of those finances. The fund financial statements provide the next level of detail. For governmental activities, these statements tell how services were financed in the short term, as well as what remains for future spending. The fund financial statements look at the EAA's operations in more detail than the government-wide financial statements by providing information about the EAA's most significant fund: the General Fund. The remaining statement, the statement of fiduciary assets and liabilities, presents financial information about activities for which the EAA acts solely as an agent for the benefit of students and parents. Below is an outline of the report format:

Management's Discussion and Analysis (MD&A)
(Required Supplemental Information)

Basic Financial Statements

Government-wide Financial Statements Fund Financial Statements

Notes to the Basic Financial Statements

Required Supplemental Information
Budgetary Information for Major Fund

Reporting the Authority as a Whole - Government-wide Financial Statements

One of the most important questions asked about the School District is, "As a whole, what is the EAA's financial condition as a result of the year's activities?" The statement of net position and the statement of activities, which appear first in the EAA's financial statements, report information on the School District as a whole and its activities in a way that helps you answer this question. We prepare these statements to include all assets and liabilities, using the accrual basis of accounting, which is similar to the accounting used by most private sector companies. All of the current year's revenue and expenses are taken into account, regardless of when cash is received or paid. These two statements report the EAA's net position - the difference between assets and liabilities, as reported in the statement of net position - as one way to measure the EAA's financial health or financial position. Over time, increases or decreases in the EAA's net position, as reported in the statement of activities, are indicators of whether its financial health is improving or deteriorating. The relationship between revenue and expenses is the EAA's operating results.

Education Achievement Authority

Management's Discussion and Analysis (Continued)

However, the EAA's goal is to provide services to our students, not to generate profits as commercial entities do. One must consider many other nonfinancial factors, such as the quality of the education provided and the safety of the schools, to assess the overall health of the Authority. The statement of net position and the statement of activities report the governmental activities for the School District, which encompass all of its services, including instruction, support services, community services, and athletics. Unrestricted state aid revenue (based on the foundation allowance and student enrollment) and state and federal grants finance most of these activities.

Reporting the EAA's Most Significant Funds - Fund Financial Statements

The EAA's fund financial statements provide detailed information about the most significant funds - not the EAA as a whole. Some funds are required to be established by state law. However, the EAA can establish many other funds to help it control and manage money for specific purposes or to show that it is meeting legal responsibilities for using certain grants and other money. The governmental funds of the EAA use the following accounting approach:

Governmental Funds - All of the EAA's services are reported in governmental funds. Governmental fund reporting focuses on showing how money flows into and out of funds and the balances left at year end that are available for future spending. They are reported using the modified accrual accounting method, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the operations of the Authority and the services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the EAA's programs. We describe the relationship (or differences) between governmental activities (reported in the statement of net position and the statement of activities) and governmental funds in a reconciliation.

Education Achievement Authority

Management's Discussion and Analysis (Continued)

The EAA as a Whole

Recall that the statement of net position provides the perspective of the EAA as a whole. Table I provides a summary of the EAA's net assets as of June 30, 2016 and 2015:

Table I	Governmental Activities	
	June 30	
	2016	2015
	(in thousands)	
Assets		
Current and other assets	\$ 19,477.1	\$ 18,568.3
Capital assets	<u>5,627.2</u>	<u>8,559.9</u>
Total assets	25,104.3	27,128.2
Liabilities		
Current liabilities	11,502.4	18,632.7
Long-term liabilities	<u>-</u>	<u>2,660.3</u>
Total liabilities	<u>11,502.4</u>	<u>21,293.0</u>
Net Position		
Invested in capital assets - Net of related debt	5,064.1	7,111.9
Restricted	-	38.0
Unrestricted	<u>8,537.8</u>	<u>(1,314.7)</u>
Total net position	<u>\$ 13,601.9</u>	<u>\$ 5,835.2</u>

Total net position was \$13.6 million at June 30, 2016. Net investment in capital assets of \$5.1 million represents the original cost of the assets less accumulated depreciation less the debt used to finance the acquisition of those assets. The debt consists of a computer equipment lease and will be repaid from standard operating funds. The remaining amount of net position consists of \$8.5 million of unrestricted assets and represents the accumulated results of all past years' operations. Restricted net assets (2015) are resources remaining to be spent on grants that were received by the EAA that are restricted in purpose. These resources can only be spent on functions specified in the grant agreements. The unrestricted net asset balance is used for working capital and cash flow requirements as well as to provide for future uncertainties. The operating results of the General Fund will have a significant impact on the change in unrestricted net assets from year to year. The results of operations for the EAA, as a whole, are reported in the statement of activities (see Table 2).

Education Achievement Authority

Management's Discussion and Analysis (Continued)

Table 2

	Governmental Activities	
	Year Ended June 30	
	2016	2015
	(in thousands)	
Revenue		
Program revenue:		
Federal grants and entitlements	\$ 23,078.2	\$ 21,992.6
State categoricals	5,317.4	6,747.0
Operating grants	-	-
Special millage	82.9	-
General revenue:		
State aid	41,939.8	46,564.0
Interest and investment earnings	-	0.2
Loss on sale of capital assets	-	(3.4)
Local and other revenue	810.1	1,912.3
Total revenue	<u>71,228.4</u>	<u>77,212.7</u>
Functions/Program Expenses		
Instruction	25,407.5	28,983.8
Support services	33,381.4	49,439.4
Athletics	556.0	518.3
Community services	926.7	924.5
Interest on long-term debt	27.6	51.4
Depreciation (unallocated)	3,162.5	3,134.5
Total functions/program expenses	<u>63,461.7</u>	<u>83,051.9</u>
Increase (Decrease) in Net Position	7,766.7	(5,839.2)
Net Position - Beginning of year	<u>5,835.2</u>	<u>11,674.4</u>
Net Position - End of year	<u><u>\$ 13,601.9</u></u>	<u><u>\$ 5,835.2</u></u>

As reported in the statement of activities, the cost of all educational activities this year was approximately \$63.5 million. These activities were funded primarily with non-restricted pupil-based state aid of \$41.9 million, restricted government grants and contributions of \$28.5 million, and other sources of \$0.8 million.

The EAA experienced an increase in net position of approximately \$7.8 million. This is primarily due to the restructure and waiver of its remaining 2015 and 2016 obligation for Detroit Public Schools rent and services.

Education Achievement Authority

Management's Discussion and Analysis (Continued)

The EAA's Funds

As noted earlier, the EAA uses funds to help it control and manage money for specific purposes. Fund financial statements provide the reader with information needed to determine whether the EAA is being accountable for the resources taxpayers and others provide to it and may provide more insight into the EAA's overall financial health.

At June 30, 2016, the General Fund had a fund balance of approximately \$10.0 million, which is an increase of \$9.5 million from last year. The increase was primary due to the waiver of the EAA's share of Detroit Public Schools' debt (a component of rent expense) by the State of Michigan in connection with the state legislature's financing package of the Detroit Public Schools.

Unassigned fund balance is available to help fund the cost of operating the District.

General Fund Budgetary Highlights

Over the course of the year, the EAA revises its budget as variables that were estimated in the original budget become known. Budgeted revenue was adjusted to reflect state aid for actual pupil enrollment and grant funds and budgeted expenditures were adjusted to align with available revenue. State law requires that the budget be amended to ensure expenditures do not exceed appropriations. The final amendment to the budget was adopted in June 2016, just prior to year end. A schedule showing the EAA's original and final budget amounts compared with actual results is provided in the required supplemental information section of these financial statements.

The waiver of the EAA's share of the Detroit Public Schools' debt obligation (reflected in operations and maintenance) was not known at the time of the budget amendment. This event contributed to the favorable variance in this functional area.

Capital Assets and Debt Administration

Capital Assets

As of June 30, 2016 and 2015, the EAA had approximately \$5.6 million and \$8.6 million, respectively, invested in a broad range of capital assets, including improvements to school buildings, furniture and equipment, vehicles, and computer equipment. This amount represents a net decrease (including additions, disposals, and depreciation) of approximately \$3.0 million from last year.

Education Achievement Authority

Management's Discussion and Analysis (Continued)

	2016	2015
Buildings and building improvements	\$ 10,041,004	\$ 10,041,004
Furniture and equipment	2,712,640	2,482,790
Computer equipment	<u>3,530,650</u>	<u>3,530,650</u>
Total capital assets	16,284,294	16,054,444
Less accumulated depreciation	<u>10,657,073</u>	<u>7,494,561</u>
Net capital assets	<u><u>\$ 5,627,221</u></u>	<u><u>\$ 8,559,883</u></u>

Debt

At the end of this year, the Authority had no bonds outstanding.

Other obligations included capital leases for computer equipment and employee compensated absences.

Economic Factors and Next Year's Budgets and Rates

The EAA board and administration consider many factors when setting the 2017 fiscal year original budget. One of the most important factors affecting the budget is student enrollment. The state foundation revenue is determined by multiplying the blended student count by the per pupil foundation allowance. The blended count for the 2017 fiscal year is based on a weighted average of 90 percent of the October 2016 student count and 10 percent of the February 2016 count. The fiscal year 2017 original budget was adopted in June 2016, based on an estimate of students that will be enrolled. It is anticipated that the fall student count will be slightly lower than actual 2016 enrollment. Once the actual fall student count, related per-pupil funding, and other variables are known, the EAA will revise the budget.

Approximately 61 percent of total General Fund revenue is from the foundation allowance. Under state law, the EAA cannot levy property taxes to fund its operations. As a result, its funding is heavily dependent on the State's ability to fund local school operations. The State periodically holds a revenue-estimating conference to estimate revenue. Based on the results of the most recent conference, the State estimates there is sufficient revenue to fund the appropriation.

The EAA will cease operations at June 30, 2017 as part of the 2016 reorganization of the Detroit Public Schools. Administration is in discussion with officials from the State of Michigan and the new Detroit Public Schools Community District on a plan of transition whereby EAA schools are returned to the Detroit Public Schools Community District.

Education Achievement Authority

Management's Discussion and Analysis (Continued)

Contacting the School District's Management

This financial report is intended to provide stakeholders with a general overview of the School District's finances and to show the School District's accountability for the money it receives. If you have any questions about this report or need additional information, we welcome you to contact the business office.

Education Achievement Authority

Statement of Net Position June 30, 2016

	Governmental Activities
Assets	
Cash (Note 3)	\$ 6,457,670
Receivables (Note 4):	
Accounts receivable	369,686
Due from other governmental units	12,575,281
Prepaid assets	74,402
Capital assets - Net (Note 5)	<u>5,627,221</u>
Total assets	25,104,260
Liabilities	
Accounts payable	5,899,378
Accrued payroll-related liabilities	1,957,347
Accrued interest	1,657
Contingent liability (Note 13)	1,049,017
Unearned revenue (Note 4)	937,329
Noncurrent liabilities -	
Due within one year (Note 7)	<u>1,657,634</u>
Total liabilities	<u>11,502,362</u>
Net Position	
Net investment in capital assets	5,064,058
Unrestricted	<u>8,537,840</u>
Total net position	<u><u>\$ 13,601,898</u></u>

Education Achievement Authority

Statement of Activities Year Ended June 30, 2016

	Expenses	Program Revenue	Governmental Activities
		Operating Grants and Contributions	Net (Expense) Revenue and Changes in Net Position
Functions/Programs			
Primary government - Governmental activities:			
Instruction	\$ 25,407,512	\$ 11,670,942	\$ (13,736,570)
Support services	33,381,424	15,888,286	(17,493,138)
Athletics	556,013	-	(556,013)
Community services	926,639	919,229	(7,410)
Interest (Note 7)	27,565	-	(27,565)
Depreciation expense (unallocated) (Note 5)	3,162,512	-	(3,162,512)
Total primary government	<u>\$ 63,461,665</u>	<u>\$ 28,478,457</u>	(34,983,208)
			General revenue:
			State aid not restricted to specific purposes
			41,939,820
			Local grants and other unrestricted revenue
			<u>810,097</u>
			Total general revenue
			<u>42,749,917</u>
			Change in Net Position
			7,766,709
			Net Position - Beginning of year
			<u>5,835,189</u>
			Net Position - End of year
			<u>\$ 13,601,898</u>

Education Achievement Authority

Governmental Fund Balance Sheet June 30, 2016

	<u>General Fund</u>
Assets	
Cash (Note 3)	\$ 6,457,670
Receivables (Note 4):	
Accounts receivable	369,686
Due from other governmental units	12,575,281
Due from other funds (Note 6)	62,095
Prepaid assets	74,402
	<u> </u>
Total assets	<u>\$ 19,539,134</u>
Liabilities, Deferred Inflows of Resources, and Fund Balance	
Liabilities	
Accounts payable	\$ 5,961,473
Accrued payroll-related liabilities	1,957,347
Unearned revenue (Note 4)	937,329
	<u> </u>
Total liabilities	8,856,149
Deferred Inflows of Resources - Unavailable revenue (Note 4)	729,708
	<u> </u>
Total liabilities and deferred inflows of resources	9,585,857
Fund Balance	
Nonspendable - Prepaid assets	74,402
Assigned - Budgeted use of fund balance in subsequent year	2,937,604
Unassigned	6,941,271
	<u> </u>
Total fund balance	9,953,277
	<u> </u>
Total liabilities, deferred inflows of resources, and fund balance	<u>\$ 19,539,134</u>

Education Achievement Authority

Governmental Fund Reconciliation of the Balance Sheet of Governmental Fund to the Statement of Net Position June 30, 2016

Fund Balance Reported in Governmental Fund	\$	9,953,277
Amounts reported for governmental activities in the statement of net position are different because:		
Capital assets used in governmental activities are not financial resources and are not reported in the funds:		
Cost of capital assets	\$ 16,284,294	
Accumulated depreciation	<u>(10,657,073)</u>	5,627,221
Long-term liabilities are not due and payable in the current period and are not reported in the governmental funds:		
Net capital leases	(563,163)	
Employee compensated absences	<u>(1,094,471)</u>	(1,657,634)
Accrued interest payable is not included as a liability in governmental funds		(1,657)
Grant reimbursements not available to pay current period expenditures are deferred in the governmental funds		729,708
Contingent liabilities are recorded when matured (due and payable) in the governmental funds, but are recorded when estimable and probable in the statement of net position		<u>(1,049,017)</u>
Net Position of Governmental Activities	\$	<u>13,601,898</u>

Education Achievement Authority

Governmental Fund Statement of Revenue, Expenditures, and Changes in Fund Balance Year Ended June 30, 2016

	<u>General Fund</u>
Revenue	
Local sources	\$ 828,468
State sources	47,257,197
Federal sources	22,381,137
Interdistrict sources	<u>82,875</u>
Total revenue	70,549,677
Expenditures	
Current:	
Instruction	25,706,657
Support services	32,946,792
Athletics	556,013
Community services	928,536
Debt service:	
Principal (Note 7)	884,800
Interest	<u>30,277</u>
Total expenditures	<u>61,053,075</u>
Net Change in Fund Balance	9,496,602
Fund Balance - Beginning of year	<u>456,675</u>
Fund Balance - End of year	<u><u>\$ 9,953,277</u></u>

Education Achievement Authority

Governmental Fund Reconciliation of the Statement of Revenue, Expenditures, and Changes in Fund Balance of Governmental Fund to the Statement of Activities Year Ended June 30, 2016

Net Change in Fund Balance - Governmental Fund \$ 9,496,602

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

Governmental funds report capital outlays as expenditures; however, in the statement of activities, these costs are allocated over their estimated useful lives as depreciation:

Depreciation expense	\$ (3,162,512)	
Capitalized capital outlay	<u>229,850</u>	(2,932,662)

Revenue is reported in the statement of activities when earned; it is not reported in the funds until collected or collectible within 60 days of year end 678,697

Contingent liabilities are recorded when matured (due and payable) in the governmental funds, but are recorded when estimable and probable in the statement of net position (481,330)

Repayment of capital lease principal is an expenditure in the governmental funds, but not in the statement of activities (where it reduces long-term debt) 884,800

Interest expense is recorded in the statement of activities when incurred; it is not reported in governmental funds until paid 2,712

Compensated absences are recorded when earned in the statement of activities. In the current year, less was earned than paid out 117,890

Change in Net Position of Governmental Activities \$ 7,766,709

Education Achievement Authority

Fiduciary Funds Statement of Fiduciary Assets and Liabilities June 30, 2016

	Agency Funds
Assets - Cash (Note 3)	<u>\$ 219,222</u>
Liabilities	
Accounts payable	\$ 156,986
Due to student activities	141
Due to other funds (Note 6)	<u>62,095</u>
Total liabilities	<u>\$ 219,222</u>

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note 1 - Nature of Business and Significant Accounting Policies

The Education Achievement Authority (the "EAA," the "Authority," or the "School District") is a public school district formed by an interlocal agreement between Detroit Public Schools (DPS) and Eastern Michigan University. Its purpose is to assume the operations and assets of the lowest performing schools within the state of Michigan. The State has granted legal authority to the Authority to operate as a school district within the boundaries of the city of Detroit for an initial term of 15 years with automatic extensions in five-year increments.

Under the terms of the interlocal agreement, Eastern Michigan University may withdraw from the agreement on the first June 30 after providing at least 180 days' notice of the intent to withdraw provided the notice is provided after December 30, 2014 or another state public university is admitted to be a party to the agreement. In the event Eastern Michigan University withdraws from the agreement and the agreement is not amended to allow for another public school district or state public university to participate in the agreement, the legal basis for the Authority to operate would cease. As of February 5, 2016, Eastern Michigan University decided to withdraw from the Interlocal Agreement and the Authority will cease operations as of June 30, 2017. No other public school district or public university will participate in the agreement, thereby causing the cessation of operations at June 30, 2017. At that time, the leased buildings will be returned back to the Detroit Public Schools Community District.

The Authority was formed in August 2011; however, the Authority began actively operating and managing the 12 selected schools and receiving state foundation allowance during the fiscal year beginning July 1, 2012.

Effective August 9, 2012, the Authority granted a charter to operate three schools as a separate public school academy. The academy is recognized as an independent district by the State of Michigan and is governed by an independent board. The EAA acts as the fiscal agent to the academy and is accountable for providing oversight and compliance monitoring. The academy provides the EAA an oversight fee equal to 3 percent of the academy's annual per-pupil state revenue and pays additional fees for certain administrative support services provided by the EAA.

The Education Achievement Authority conforms to accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. The following is a summary of the significant accounting policies used by the Authority:

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note I - Nature of Business and Significant Accounting Policies (Continued)

Reporting Entity

The Authority is governed by an 11-member Board of Education appointed by the governor of Michigan, Eastern Michigan University, and DPS. The accompanying financial statements have been prepared in accordance with criteria established by the Governmental Accounting Standards Board for determining the various governmental organizations to be included in the reporting entity. These criteria include significant operational financial relationships that determine which of the governmental organizations are a part of the Authority's reporting entity, and which organizations are legally separate component units of the Authority. Based on the application of the criteria, the Authority does not contain any component units.

Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net position and the statement of activities) report information on all of the nonfiduciary activities of the primary government. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by intergovernmental revenue, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. All of the Authority's government-wide activities are considered governmental activities.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenue. Direct expenses are those that are clearly identifiable with a specific function. Program revenue includes grants and contributions that are restricted to meeting the operational requirements of a particular function. Intergovernmental payments, unrestricted grants, and other items not properly included among program revenue are reported instead as general revenue.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

Government-wide Financial Statements - The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants, categorical aid, and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

As a general rule, the effect of interfund activity has been eliminated from the government-wide financial statements.

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note I - Nature of Business and Significant Accounting Policies (Continued)

When an expense is incurred for purposes for which both restricted and unrestricted net position or fund balance are available, the Authority's policy is to first apply restricted resources. When an expense is incurred for purposes which amounts in any of the unrestricted fund balance classifications could be used, it is the Authority's policy to spend funds in this order: committed, assigned, and unassigned.

Amounts reported as program revenue include operating grants and contributions. Internally dedicated resources are reported as general revenue rather than as program revenue. Likewise, general revenue includes all unrestricted state aid and local grants.

Fund Financial Statements - Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is collected within the current period or soon enough thereafter to pay liabilities of the current period. Revenue not meeting this definition is classified as a deferred inflow of resources. For this purpose, the Authority considers revenue to be available if it is collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Unrestricted state aid, intergovernmental grants, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenue of the current fiscal period. All other revenue items are considered to be available only when cash is received by the Authority.

Fiduciary fund statements are also reported using the economic resources measurement focus and the accrual basis of accounting.

The Authority reports the following major governmental fund:

General Fund - The General Fund is the Authority's primary operating fund. It accounts for all financial resources of the Authority, except those required to be accounted for in another fund.

Additionally, the Authority reports the following fund type:

Student Activities Agency Fund - The Authority presently maintains an Agency Fund to record the transactions of student groups for school and school-related purposes. The funds are segregated and held in trust for the students.

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note I - Nature of Business and Significant Accounting Policies (Continued)

Assets, Liabilities, and Net Position or Equity

Receivables and Payables - In general, outstanding balances between funds are reported as “due to/from other funds.” Activities between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as “advances to/from other funds.”

All trade and grant receivables are shown net of an allowance for uncollectible amounts. The Authority considers all receivables to be fully collectible; accordingly, no allowance for uncollectible amounts is recorded.

Prepaid Costs - Certain payments to vendors reflect costs applicable to future fiscal years and are recorded as prepaid costs in both government-wide and fund financial statements.

Capital Assets - Capital assets, which include building improvements, equipment, and vehicles, are reported in the governmental column in the government-wide financial statements. Capital assets are defined by the Authority as assets with an initial individual cost of more than \$5,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. Costs of normal repair and maintenance that do not add to the value or materially extend asset life are not capitalized. The Authority does not have infrastructure-type assets.

Buildings and building additions represent improvements to leased buildings and are depreciated over the life of the lease. Buildings, equipment, and vehicles are depreciated using the straight-line method over the following useful lives:

Buildings and building additions	5 years
Vehicles	5 years
Furniture and other equipment	5 to 20 years

Compensated Absences (Vacation and Sick Leave) - The liability for compensated absences reported in the government-wide statements consists of earned but unused accumulated vacation and sick leave benefits. A liability for these amounts is reported in governmental funds as it comes due for payment. The liability has been calculated using the vesting method, in which leave amounts for both employees who are currently eligible to receive termination payments at normal retirement age and other employees who are expected to become eligible in the future to receive such payments upon normal retirement are included.

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

Long-term Obligations - In the government-wide financial statements, long-term obligations, which include capital lease obligations, are reported as liabilities in the statement of net position.

In the fund financial statements, governmental fund types recognize capital lease payments as debt service expenditures during the current period.

Deferred Outflows/Inflows of Resources - In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element represents a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (expense/expenditure) until then. The Authority does not have any items that qualify for reporting in this category.

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element represents an acquisition of net position that applies to a future period and so will not be recognized as an inflow of resources (revenue) until that time. The Authority has only one type of item, which arises only under a modified accrual basis of accounting, that qualifies for reporting in this category.

Accordingly, the item, unavailable revenue, is reported only in the governmental funds balance sheet. The governmental funds report unavailable revenue from amounts due from other governments and other granting agencies that are not considered available. These amounts are deferred and recognized as an inflow of resources in the period that the amounts become available.

Fund Balance - In the fund financial statements, governmental funds report the following components of fund balance:

- **Nonspendable:** Amounts that are not in spendable form or are legally or contractually required to be maintained intact
- **Restricted:** Amounts that are legally restricted by outside parties, constitutional provisions, or enabling legislation for use for a specific purpose
- **Committed:** Amounts that have been formally set aside by the Board of Education for use for specific purposes. Commitments are made and can be rescinded only via resolution of the board of directors.
- **Assigned:** Intent to spend resources on specific purposes expressed by the board of directors

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note 1 - Nature of Business and Significant Accounting Policies (Continued)

- **Unassigned:** Amounts that do not fall into any other category above. This is the residual classification for amounts in the General Fund and represents fund balance that has not been assigned to other funds and has not been restricted, committed, or assigned to specific purposes in the General Fund. In other governmental funds, only negative unassigned amounts are reported, if any, and represent expenditures incurred for specific purposes exceeding the amounts previously restricted, committed, or assigned to those purposes.

Use of Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

Comparative Data - Comparative data is not included in the Authority's financial statements.

Note 2 - Stewardship, Compliance, and Accountability

Budgetary Information - Annual budgets are adopted on a basis consistent with generally accepted accounting principles and state law for the General Fund. All annual appropriations lapse at fiscal year end.

The budget document presents information by fund and function. The legal level of budgetary control adopted by the governing body (i.e., the level at which expenditures may not legally exceed appropriations) is the function level. The statement of revenue, expenditures, and changes in fund balance also presents capital outlay within the functions due to the limited amount within each function. State law requires the Authority to have its budget in place by July 1. Expenditures in excess of amounts budgeted are a violation of Michigan law. State law permits districts to amend their budgets during the year. During the year, the budget was amended in a legally permissible manner.

Encumbrance accounting is employed in governmental funds. Encumbrances (e.g., purchase orders, contracts) outstanding at year end are reported as restrictions, commitments, or assignments of fund balances and do not constitute expenditures or liabilities because the goods or services have not been received as of year end; the commitments will be reappropriated and honored during the subsequent year.

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note 2 - Stewardship, Compliance, and Accountability (Continued)

The Authority budgets and reports athletics expenditures within the support services - central function in the budgetary comparison schedule - General Fund. Additionally, within the original budget, the Authority budgeted debt service expenditures related to its capital lease for computer equipment within the support services - instructional staff function. The Authority budgeted for these debt service expenditures separately within the amended budget. In accordance with generally accepted accounting principles, the Authority reports these items in the proper functions in the statement of revenue, expenditures, and changes in fund balance. Beginning fund balance for the original budget in the budgetary comparison schedule has been reflected as the estimated beginning fund balance used when adopting the original budget, as opposed to the actual beginning fund balance.

Excess of Expenditures Over Appropriations in Budgeted Funds - During the year, the Authority incurred expenditures in the General Fund which were in excess of the amounts budgeted, as follows:

	<u>Budget</u>	<u>Actual</u>
School administration	\$ 3,731,507	\$ 3,881,204

Note 3 - Deposits and Investments

State statutes authorize the Authority to make deposits in the accounts of federally insured banks, credit unions, and savings and loan associations that have offices in Michigan. The Authority is allowed to invest in U.S. Treasury or agency obligations, U.S. government repurchase agreements, bankers' acceptances, commercial paper rated prime at the time of purchase that matures not more than 270 days after the date of purchase, mutual funds, and investment pools that are composed of authorized investment vehicles. The Authority's deposits are in accordance with statutory authority.

The Authority has designated two banks for the deposit of its funds.

The Authority's cash and investments are subject to custodial credit risk, which is examined in more detail below:

Custodial Credit Risk of Bank Deposits - Custodial credit risk is the risk that in the event of a bank failure, the Authority's deposits may not be returned to it. The Authority does not have a deposit policy for custodial credit risk. At year end, the School District's deposit balance of \$7,016,367 had \$6,516,637 of bank deposits (checking and money market demand account) that were uninsured and uncollateralized. The Authority evaluates each financial institution with which it deposits funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note 4 - Receivables and Unavailable/Unearned Revenue

The majority of the intergovernmental receivable is from the State of Michigan for the July and August state aid payments and from the federal government for grants. Accounts receivable are amounts due to the Authority primarily from charter schools authorized by the Authority for payment of invoices on behalf of the charters. These amounts were fully collected subsequent to June 30, 2016.

Governmental funds report unavailable revenue in connection with receivables for revenue that is not considered to be available to liquidate liabilities of the current period. Governmental funds also report unearned revenue in connection with resources that have been received but not yet earned. At the end of the current fiscal year, the various components of unearned and unavailable revenue are as follows:

	<u>Governmental Funds</u>	
	<u>Deferred</u>	
	Inflow -	Liability -
	<u>Unavailable</u>	<u>Unearned</u>
Grant reimbursements and pledges received after the period of availability	\$ 729,708	\$ -
Grant and categorical aid payment received prior to meeting all eligibility requirements	-	937,329

Note 5 - Capital Assets

Capital asset activity of the Authority's governmental activities was as follows:

Governmental Activities	<u>Balance</u> July 1, 2015	<u>Additions/</u> <u>Transfers</u>	<u>Disposals/</u> <u>Transfers</u>	<u>Balance</u> June 30, 2016
Capital assets being depreciated:				
Buildings and improvements	\$ 10,041,004	\$ -	\$ -	\$ 10,041,004
Furniture and equipment	2,482,790	229,850	-	2,712,640
Computer equipment (capital lease)	3,530,650	-	-	3,530,650
Subtotal	16,054,444	229,850	-	16,284,294
Accumulated depreciation:				
Buildings and improvements	5,013,520	2,008,201	-	7,021,721
Furniture and equipment	715,716	448,181	-	1,163,897
Computer equipment (capital lease)	1,765,325	706,130	-	2,471,455
Subtotal	7,494,561	3,162,512	-	10,657,073
Net capital assets being depreciated	8,559,883	(2,932,662)	-	5,627,221
Net capital assets	<u>\$ 8,559,883</u>	<u>\$ (2,932,662)</u>	<u>\$ -</u>	<u>\$ 5,627,221</u>

Depreciation expense was not charged to activities as the Authority considers its assets to impact multiple activities and allocation is not practical.

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note 6 - Interfund Receivables, Payables, and Transfers

At June 30, 2016, the Agency Fund has recorded a due to the General Fund for \$62,095. This balance results from the time lag between the dates that goods and services are provided or reimbursable expenditures occur, transactions are recorded in the accounting system, and payments between funds are made.

Note 7 - Long-term Debt

The Authority issues notes and other contractual commitments to provide for the acquisition of certain equipment. Notes, installment purchase agreements, and capital leases are also general obligations of the Authority. Other obligations include compensated absences.

Long-term debt activity can be summarized as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Governmental Activities					
Capital leases	\$ 1,447,963	\$ -	\$ 884,800	\$ 563,163	\$ 563,163
Employee compensated absences	1,212,361	-	117,890	1,094,471	1,094,471
Total governmental activities	<u>\$ 2,660,324</u>	<u>\$ -</u>	<u>\$ 1,002,690</u>	<u>\$ 1,657,634</u>	<u>\$ 1,657,634</u>

Total interest expense recognized in the government-wide financial statements for the year ended June 30, 2016 was \$27,565.

Capital Leases - The Authority has entered into lease agreements as lessee for financing the purchase of certain computer equipment. These lease agreements qualify as capital leases for accounting purposes and therefore have been recorded in the government-wide statements at the present value of the future minimum lease payments as of the inception date. The property acquired under the lease agreements is included in Note 5. The future minimum lease obligations and the net present value are as follows:

Year Ending <u>June 30</u>	<u>Amount</u>
2017	\$ 570,017
Less amount representing interest	<u>6,854</u>
Present value of net minimum lease payments	<u>\$ 563,163</u>

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note 8 - Local Revenue

In addition to the state aid awarded and federal grant revenue as discussed in Note 1, the Authority also received certain funding from private, local sources for the year ended June 30, 2016. The most significant private source was as follows:

Kellogg Foundation Grant - A \$500,000 grant was awarded for general operating support. As of June 30, 2016, the Authority had received all funds related to this grant, and had met the eligibility requirements for 100 percent of the grant award.

Note 9 - Operating Leases

The Authority began leasing 15 school buildings in the fiscal year ended June 30, 2013 with DPS, with three of the buildings being subleased to charter schools for \$1 per year each. The Authority is leasing the buildings from the original district at a rate of \$1 per annum plus the number of Detroit resident students attending each school multiplied by \$910 per year for the period of three years from the commencement date of the signed lease agreement. The Authority has annual options to renew the term for successive one-year periods, which the Authority executed during the year and extended the leases through June 30, 2016.

Rent was to be charged for non-Detroit resident students at the lesser of (a) 2.5 percent of the Academy's total annual state aid revenue for students attending school or (b) an amount equal to 10 percent of the square footage of the building times \$1 times 12 months.

The Authority assumes all responsibility to manage all of the assets leased according to all applicable federal and state program rules and regulations.

The lease also provides a provision that any money expended by the Authority to make alterations, improvements, or additions to the buildings necessary to enable the Authority to utilize them will be deducted from the lease payment amount. Normal repairs and maintenance are paid for by the Authority. For the year ended June 30, 2016, \$1,000,000 was paid by the Authority to DPS for rent associated with the 2014-2015 year end. Remaining rent balances of approximately \$4.5 million have been waived relating to outstanding balances associated with the June 30, 2015 rent amounts. Both parties have agreed that no rent will be charged for the year ended June 30, 2016.

Rent for the facilities for the year ending June 30, 2017 will be \$1,618,749 and will be paid for beginning July 2016 through July 2017.

The Authority also began leasing a building for their administrative office space during the fiscal year ended June 30, 2013 for a period of five years from the commencement date of the signed lease agreement. The Authority has one five-year renewal option at the end of the initial lease term.

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note 9 - Operating Leases (Continued)

Total cost for the administrative office lease was approximately \$132,500 for the year ended June 30, 2016.

The administrative office space lease expires in 2018. Given the non-renewal of the Authority charter, it is unknown if the Authority will be liable for the final year of the lease as the Authority will cease operations at June 30, 2017. Under the terms of the lease agreement, future minimum lease payments are as follows:

Years Ending June 30	Amount
2017	\$ 135,000
2018	137,500
Total	\$ 272,500

Note 10 - Related Party Transactions

DPS and Eastern Michigan University - The Authority has related party relationships with DPS and Eastern Michigan University due to the interlocal agreement signed between the Board of Regents of Eastern Michigan University and the School District for the City of Detroit creating the Education Achievement Authority signed on July 14, 2011. During the year ended June 30, 2016, the Authority contracted with DPS for certain IT management, security, and other services. The total amount due to DPS during the year ended June 30, 2016 for these services is approximately \$1,393,000. As of November 4, 2016, the Authority and DPS agreed to waive those fees and to then charge an amount of \$831,000 for these same services for the fiscal year ending June 30, 2017. The amount for services of \$831,000 for the year ending June 30, 2017 will be paid for in monthly installments through July 2017.

Additionally, DPS operates a food service activity at all EAA buildings. The results of this activity are not included in these financial statements.

During the year ended June 30, 2016, the Authority contracted with Eastern Michigan University for certain professional development services and services. The amount expended and paid to Eastern Michigan University for the year ended June 30, 2016 was \$2,850.

Michigan Educational Choice Center (MECC) - The Authority is the authorizing entity for MECC, a charter school operating in Detroit, Michigan. The Authority charges a fee equal to 3 percent of MECC's state aid. Additionally, the Authority processes certain transactions on behalf of MECC and charges a fee of 2.5 percent of the transaction. Revenue recognized from MECC during the fiscal year ended June 30, 2016 totaled approximately \$239,000.

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note 11 - Risk Management

The Authority is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The Authority has purchased commercial insurance for general business claims, medical, dental, and vision claims, as well as workers' compensation. The Authority works closely with insurance providers to address any claims that may not be covered by insurance fully or at all to assess authority exposure. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three fiscal years.

Note 12 - Defined Contribution Pension Plan

The Authority provides pension benefits to all of its full-time employees through a defined contribution plan. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings. The plan provisions and contribution requirements were established through a resolution by the Board of Education and may be amended by future board actions. Employees are eligible to participate from the date of employment and are fully vested after four years of service. The Authority matched contributions up to 7.5 percent of the employee's salary during the year ended June 30, 2016.

For the year ended June 30, 2016, employees earned \$1,027,073 of matching contributions from the Authority, of which \$115,092 remains payable as of June 30, 2016.

Note 13 - Contingent Liabilities

The Authority is required to have transactions associated with certain federal programs reviewed by a third party prior to their submission for reimbursement from the Michigan Department of Education. Due to timing of the reviews and responses by the Authority, expenditures were reimbursed prior to the final conclusions by the third party. This reimbursement was done with the approval of the Michigan Department of Education. There are several months of expenditure reviews whereby the third party has requested additional information or is waiting for information in order to resolve their questions. As a result, it is possible that certain expenditures that were reimbursed may be determined to be disallowed. Upon finalization of the third-party review, there may be funds that will need to be returned to the Michigan Department of Education, or a reduction in future grant awards. As of June 30, 2016, the dollar amounts of any possible disallowed costs are not known.

Education Achievement Authority

Notes to Financial Statements June 30, 2016

Note 13 - Contingent Liabilities (Continued)

In addition to the above expenditures, the Authority received reimbursement for expenditures incurred while administering programs funded with federal grants in a prior year that may be disallowed upon review of the granting agency. Certain material instances of noncompliance with grant requirements were identified during the Authority's June 30, 2014 A-133 federal program audit. In the event that the expenditures are ultimately disallowed, the Authority could be required to repay the amounts received as reimbursement. The Authority has recorded an estimate of the potential repayment in the government-wide statement of net position totaling approximately \$568,000, which has been accrued at June 30, 2016. Additionally, certain additional federal expenditures for the year ended June 30, 2014 have been identified as due back to the Michigan Department of Education, based on a communication from the State. These amounts, totalling approximately \$146,000 at June 30, 2016, have also been accrued in the government-wide statement of net position. The amount that may ultimately be repaid is currently unknown but could be material to the financial statements.

Legal Reserve - The Authority is currently involved in a number of litigation matters that have occurred during the course of operations. At June 30, 2016, a reserve of \$335,000 has been established for possible liabilities under the various legal proceedings. No conclusions have been reached as of the report date, nor have any judgments been levied. The Authority continues to monitor these matters as they progress through the legal process.

Required Supplemental Information

Education Achievement Authority

Required Supplemental Information Budgetary Comparison Schedule - General Fund Year Ended June 30, 2016

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	Over (Under) <u>Final Budget</u>
Revenue				
Local sources	\$ 4,129,824	\$ 952,560	\$ 828,468	\$ (124,092)
State sources	48,478,981	47,899,221	47,257,197	(642,024)
Federal sources	31,392,539	36,316,328	22,381,137	(13,935,191)
Interdistrict sources	50,000	82,875	82,875	-
Total revenue	84,051,344	85,250,984	70,549,677	(14,701,307)
Expenditures - Current				
Instruction:				
Basic program	18,505,522	20,112,438	16,696,912	(3,415,526)
Added needs	12,515,901	11,759,205	9,009,745	(2,749,460)
Total instruction	31,021,423	31,871,643	25,706,657	(6,164,986)
Support services:				
Pupil	6,867,337	8,256,566	6,487,471	(1,769,095)
Instructional staff	15,219,481	13,501,827	9,266,456	(4,235,371)
General administration	1,338,169	1,951,952	1,796,991	(154,961)
School administration	4,653,100	3,731,507	3,881,204	149,697
Business	866,983	822,929	703,636	(119,293)
Operations and maintenance	16,841,617	11,203,610	4,642,308	(6,561,302)
Pupil transportation services	2,127,139	2,453,294	1,664,633	(788,661)
Central	4,417,092	6,776,762	5,060,106	(1,716,656)
Total support services	52,330,918	48,698,447	33,502,805	(15,195,642)
Community services	702,159	1,207,903	928,536	(279,367)
Debt service	-	915,077	915,077	-
Total expenditures	84,054,500	82,693,070	61,053,075	(21,639,995)
Net Change in Fund Balance	(3,156)	2,557,914	9,496,602	6,938,688
Fund Balance - Beginning of year	128,757	456,675	456,675	-
Fund Balance - End of year	<u>\$ 125,601</u>	<u>\$ 3,014,589</u>	<u>\$ 9,953,277</u>	<u>\$ 6,938,688</u>