

**PETALUMA CITY SCHOOLS
COUNTY OF SONOMA
PETALUMA, CALIFORNIA**

AUDIT REPORT

JUNE 30, 2012

PETALUMA CITY SCHOOLS

JUNE 30, 2012

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FINANCIAL SECTION

STEPHEN ROATCH ACCOUNTANCY CORPORATION

Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT

Board of Education
Petaluma City Schools
Petaluma, California

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Petaluma City Schools (the "District"), as of and for the fiscal 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 Petaluma City Schools' management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and the 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 the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Petaluma City Schools, as of June 30, 2012, and the respective changes in financial position and cash flows, where applicable, thereof 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 our report dated March 6, 2013 on our consideration of Petaluma City Schools' 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 3 through 13, the budgetary comparison information on page 53, and the schedule of funding progress on page 58 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 Petaluma City Schools' financial statements as a whole. The accompanying combining fund financial statements, supplementary schedules listed in the table of contents, and the Schedule of Expenditures of Federal Awards, which is presented as required by the U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates 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 as a whole.

Stephen Roatch Accountancy Corporation

STEPHEN ROATCH ACCOUNTANCY CORPORATION
Certified Public Accountants

March 6, 2013

**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

(PREPARED BY DISTRICT MANAGEMENT)

This section of the Petaluma City Schools' annual financial report presents our discussion and analysis of the District's financial performance during the fiscal year that ended on June 30, 2012. Please read it in conjunction with the Independent Auditor's Report presented on pages 1 and 2, and the District's financial statements, which immediately follow this section.

USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The Statement of Net Assets and Statement of Activities, presented on pages 14 through 15, provide information about the activities of the District as a whole and present a longer-term view of the District's finances. The fund financial statements for governmental activities and business-type activities, presented on pages 16 through 22, provide information about how District services were financed in the short-term, and how much remains for future spending. Fund financial statements also report the District's operations in more detail than the government-wide statements by providing information about the District's most significant funds. The remaining statements provide information about activities for which the District acts solely as a trustee or agent for the benefit of those outside the District.

FINANCIAL HIGHLIGHTS

- The District's overall financial status did not change significantly during the course of the year, as total net assets decreased by less than 1%.
- Capital assets, net of depreciation, decreased \$2,765,963, due to the current year addition of \$2,387,332 of new capital assets, and the current year recognition of \$5,153,295 of depreciation expense.
- Total long-term liabilities decreased \$3,085,574, due primarily to the current year reduction of the District's liabilities related to general obligation bonds.
- On November 1, 2011, the District issued \$8,470,000 of general obligation refunding bonds for purposes of refunding a portion of the District's outstanding bonds with a principal balance of \$8,695,000, and to pay costs of issuance related to the new bonds. The refunding bonds were issued to lower the debt service requirements of the District and reduce the tax burden on the property owners within the District.
- The District's P-2 average daily attendance (ADA), inclusive of charter school ADA, decreased from 7,217 ADA in fiscal year 2010-11, down to 7,209 ADA in fiscal year 2011-12, a decrease of less than 1%.
- The District's General Fund incurred an operating deficit of \$281,401, and recognized a \$327,291 decrease in available reserves.
- The District maintains sufficient reserves for a district its size. It meets the state required minimum reserve for economic uncertainty of 3% of total General Fund expenditures, transfers out, and other uses (total outgo). During fiscal year 2011-12, General Fund total outgo was \$66,490,987. At June 30, 2012, the District had available reserves of \$9,774,030, which represents an available reserve of 14.7%.

**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

(PREPARED BY DISTRICT MANAGEMENT)

THE FINANCIAL REPORT

The full annual financial report consists of three separate parts, including the basic financial statements, supplementary information, and management's discussion and analysis. The three sections together provide a comprehensive overview of the District. The basic financial statements are comprised of two kinds of statements that present financial information from different perspectives, Governmental-wide and funds.

- Governmental-wide financial statements, which comprise the first two statements, provide both short-term and long-term information about the District's overall financial position.
- Individual parts of the District, which are reported as fund financial statements comprise the remaining statements.
 - ❖ Basic services funding is described in the governmental funds statements. These statements include short-term financing and identify the balance remaining for future spending.
 - ❖ Short and long-term financial information about the activities of the District that operate like businesses are provided in the proprietary fund statements.
 - ❖ Financial relationships, for which the District acts as an agent or trustee for the benefit of others to whom the resources belong, are presented in the fiduciary funds statements.

Notes to the financials, which are included in the financial statements, provide more detailed data and explain some of the information in the statements. The required supplementary information provides further explanations and provides additional support for the financial statements. A comparison of the District's budget for the year is included.

Reporting the District as a Whole

The District as a whole is reported in the Governmental-wide statements and uses accounting methods similar to those used by companies in the private sector. All of the District's assets and liabilities are included in the Statement of Net Assets. The Statement of Activities reports all of the current year's revenues and expenses regardless of when cash is received or paid.

The District's financial health or position (net assets) can be measured by the difference between the District's assets and liabilities.

- Increases or decreases in the net assets of the District over time are indicators of whether its financial position is improving or deteriorating, respectively.
- Additional non-financial factors such as the condition of school buildings and other facilities, and changes in the property tax base of the District need to be considered in assessing the overall health of the District.

In the Statement of Net Assets and the Statement of Activities, we divide the District into two kinds of activities:

**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

(PREPARED BY DISTRICT MANAGEMENT)

THE FINANCIAL REPORT (CONCLUDED)

Reporting the District as a Whole (Concluded)

Governmental Activities:

The basic services provided by the District, such as regular education, special education, and administration, are included here, and are primarily financed by state apportionments, property taxes, and other state and federal aid. Non-basic services, such as child nutrition are also included here, but are financed by a combination of state and federal programs and local revenues.

Business-type Activities:

These activities are provided on a charge for goods or services basis to recover the costs of the goods or services provided. The District's Downtown Project operations are reported as business activities.

Reporting the District's Most Significant Funds

The District's fund-based financial statements provide detailed information about the District's most significant funds. Some funds are required to be established by State law, while other funds have been established to control and manage money for specific purposes.

Governmental Funds:

The major governmental funds of the Petaluma City Schools are the General Fund and Bond Interest and Redemption Fund. Governmental fund reporting focuses on how money flows into and out of the funds and the balances that remain at the end of the year. A modified accrual basis of accounting 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 District's operations and services. Governmental fund information helps to determine the level of financial resources available in the near future to finance the District's programs.

Proprietary Funds:

Proprietary funds are activities that a District operates similar to a business, in that it attempts to recover costs through charges to the user. Proprietary funds include internal service funds and enterprise funds, and are accounted for on the full accrual basis. Internal service funds account for goods or services that are provided to other funds in return for a fee to cover the cost of operations. The District has one fund of this type, the Self-Insurance Fund. Enterprise funds are used to account for any activity or service that charges a fee to external users to cover the cost of operations. The District has one fund of this type, the Downtown Project Fund.

Fiduciary Funds:

The District is the trustee, or fiduciary, for its scholarship and student activity funds. All of the District's fiduciary activities are reported in separate fiduciary statements. We exclude these activities from the District's other financial statements because the District cannot use these assets to finance their operations. The District is responsible for ensuring that the assets reported in these funds are used for their intended purposes.

**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

(PREPARED BY DISTRICT MANAGEMENT)

FINANCIAL ANALYSIS OF THE DISTRICT AS A WHOLE

Governmental Activities:

The District's net assets decreased from \$56,075,119 at June 30, 2011, down to \$55,642,105 at June 30, 2012, a decrease of less than 1%.

Business Activities:

The District's net assets decreased from \$47,125 at June 30, 2011, down to \$34,803 at June 30, 2012, a decrease of 26%.

<u>Comparative Statement of Net Assets</u>						
	Governmental Activities		Business-Type Activities		Totals	
	2011	2012	2011	2012	2011	2012
Assets:						
Deposits and Investments	\$ 13,488,494	\$ 9,948,890	\$ 16,501	\$ 12,995	\$ 13,504,995	\$ 9,961,885
Receivables *	13,631,453	16,157,558	783	1,020	13,632,236	16,158,578
Prepaid Expenses *	1,794,688	1,473,160			1,794,688	1,473,160
Stores Inventory	59,099	59,265			59,099	59,265
Capital Assets, net	103,785,936	101,019,973	29,841	24,154	103,815,777	101,044,127
Total Assets	132,759,670	128,658,846	47,125	38,169	132,806,795	128,697,015
Liabilities:						
Current *	9,790,233	10,755,797		3,366	9,790,233	10,759,163
Long-Term *	66,894,318	62,260,944			66,894,318	62,260,944
Total Liabilities	76,684,551	73,016,741	0	3,366	76,684,551	73,020,107
Net Assets:						
Invested in Capital Assets						
- Net of Related Debt *	44,750,819	45,072,293	29,841	24,154	44,780,660	45,096,447
Restricted:						
Capital Projects *	1,737,405	1,337,337			1,737,405	1,337,337
Debt Service *	(4,183,357)	(3,938,102)			(4,183,357)	(3,938,102)
Educational Programs *	2,491,703	1,673,360			2,491,703	1,673,360
Other *	274,943	210,367			274,943	210,367
Unrestricted *	11,003,606	11,286,850	17,284	10,649	11,020,890	11,297,499
Total Net Assets *	\$ 56,075,119	\$ 55,642,105	\$ 47,125	\$ 34,803	\$ 56,122,244	\$ 55,676,908

Table includes financial data of the combined governmental funds and proprietary funds

** Prior year balances have been adjusted to ensure comparability and reflect the restatements discussed at Note 22 in these financial statements.*

The deficit balance, which is presented in the above schedule as Restricted for Debt Service, represents the amount that accumulated accreted interest on the District's outstanding capital appreciation bonds exceeds the amount that is available in the Bond Interest and Redemption Fund. This deficit will be eliminated by future property tax collections.

**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

(PREPARED BY DISTRICT MANAGEMENT)

FINANCIAL ANALYSIS OF THE DISTRICT AS A WHOLE (CONCLUDED)

Governmental Activities:

The District's total current year expenses exceeded total current year revenues and special item gain by \$433,014.

Business-Type Activities:

The District's total current year expenses exceeded total current year revenues by \$12,322.

<u>Comparative Statement of Changes in Net Assets</u>						
	<u>Governmental Activities</u>		<u>Business-Type Activities</u>		<u>Totals</u>	
	<u>2011</u>	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>	<u>2012</u>
Program Revenues:						
Charges for Services	\$ 817,028	\$ 876,740	\$ 9,525	\$ 6,480	\$ 826,553	\$ 883,220
Operating Grants & Contributions *	12,349,250	13,435,755			12,349,250	13,435,755
Capital Grants & Contributions	3,059	485				485
General Revenues:						
Taxes Levied	33,063,803	33,458,364			33,063,803	33,458,364
Federal & State Aid *	27,055,040	24,568,424			27,055,040	24,568,424
Interest & Investment Earnings	141,340	195,455	130	107	141,470	195,562
Miscellaneous	3,302,832	3,870,789			3,302,832	3,870,789
Total Revenues	76,732,352	76,406,012	9,655	6,587	76,738,948	76,412,599
Expenses:						
Instruction	44,474,359	46,486,554			44,474,359	46,486,554
Instruction-Related Services	7,395,891	7,709,482			7,395,891	7,709,482
Pupil Services	10,755,071	10,355,045			10,755,071	10,355,045
General Administration	3,207,291	3,552,516			3,207,291	3,552,516
Plant Services	6,846,894	5,915,960			6,846,894	5,915,960
Ancillary Services	340,900	326,689			340,900	326,689
Community Services	375,311	320,804			375,311	320,804
Enterprise Activities	262,743	407,367	16,709	18,909	279,452	426,276
Interest on Long-Term Debt	3,590,636	2,803,336			3,590,636	2,803,336
Other Outgo	39,648	244,536			39,648	244,536
Total Expenses	77,288,744	78,122,289	16,709	18,909	77,305,453	78,141,198
Special Item - Gain		1,283,263				1,283,263
Changes in Net Assets *	\$ (556,392)	\$ (433,014)	\$ (7,054)	\$ (12,322)	\$ (563,446)	\$ (445,336)

Table includes financial data of the combined governmental funds and proprietary funds

** Prior year balances have been adjusted to reflect the restatements discussed at Note 22 in these financial statements.*

**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

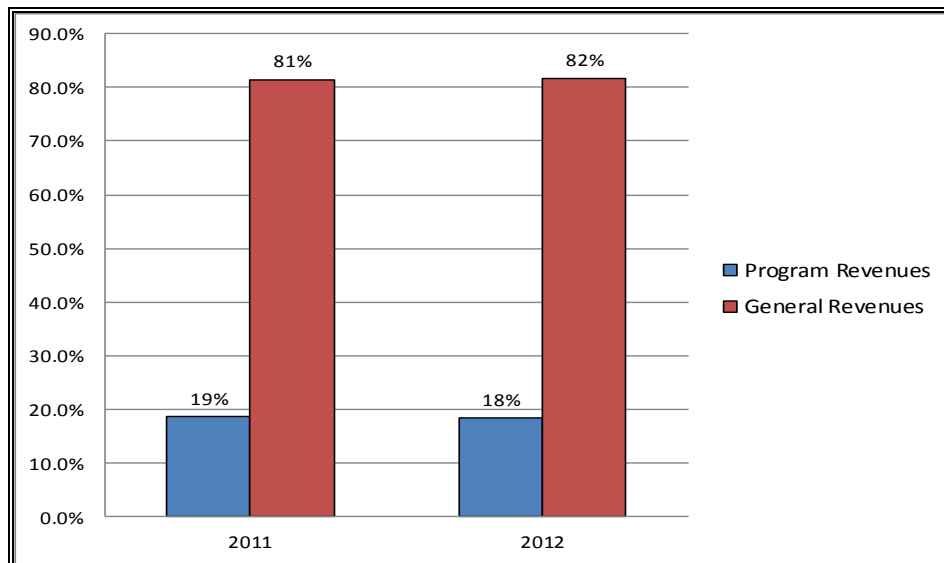
(PREPARED BY DISTRICT MANAGEMENT)

FINANCIAL ANALYSIS OF THE GOVERNMENTAL ACTIVITIES

	<u>Total Cost of Services</u>		<u>Net Cost of Services</u>	
	2011	2012	2011	2012
	Instruction	\$ 44,474,359	\$ 46,486,554	\$ 36,398,845
Instruction-Related Services	7,395,891	7,709,482	6,370,538	6,479,076
Pupil Services	10,755,071	10,355,045	5,836,339	5,759,513
General Administration	3,207,291	3,552,516	3,104,018	3,381,016
Plant Services	6,846,894	5,915,960	6,699,058	5,708,255
Ancillary Services	340,900	326,689	340,900	326,689
Community Services	375,311	320,804	375,311	320,804
Enterprise Activities	262,743	407,367	262,743	407,367
Interest on Long-Term Debt	3,590,636	2,803,336	3,590,636	2,803,336
Other Outgo	39,648	244,536	(28,101)	179,904
Totals	\$ 77,288,744	\$ 78,122,289	\$ 62,950,287	\$ 63,809,309

Table includes financial data of the combined governmental funds

The table above presents the cost of major District activities. The table also shows each activity's net cost (total cost less fees generated by the activities and intergovernmental aid provided for specific programs). The \$63,809,309 net cost represents the financial burden that was placed on the District's general revenues for providing the services listed.



Program revenues financed 18% of the total cost of providing the services listed above, while the remaining 82% was financed by the general revenues of the District.

**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

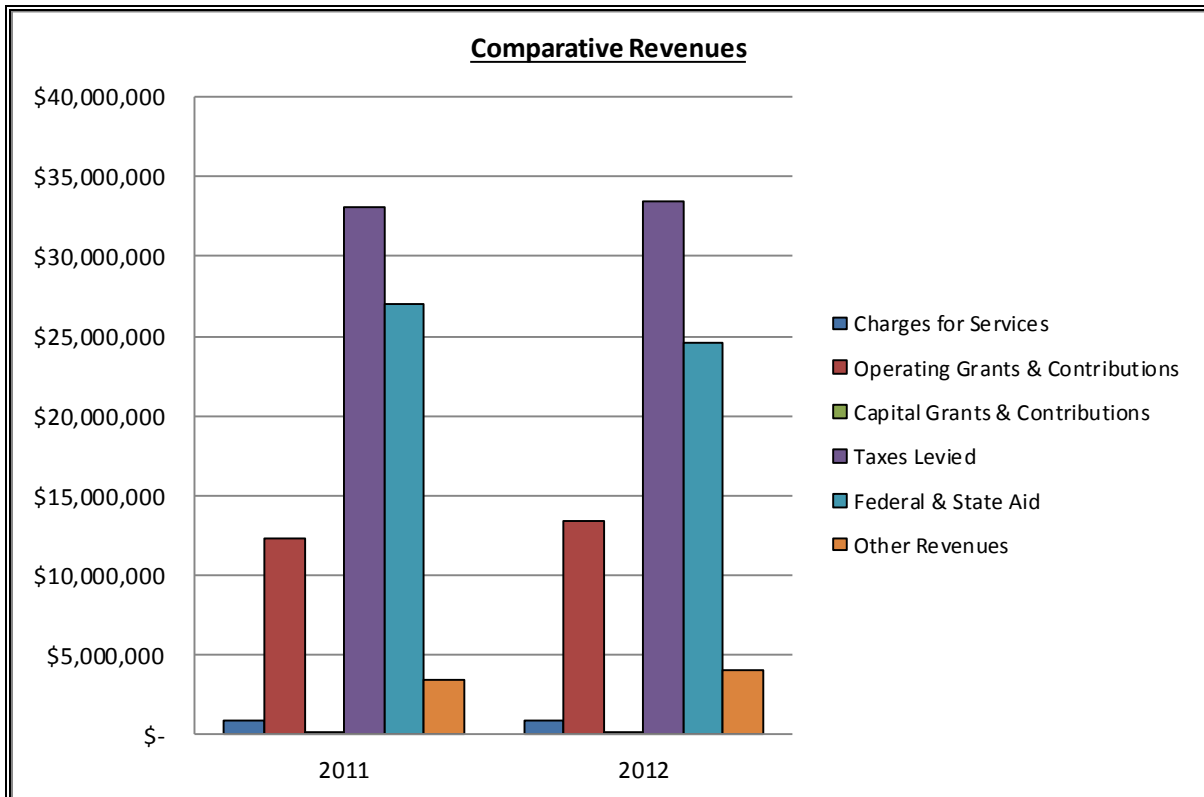
(PREPARED BY DISTRICT MANAGEMENT)

FINANCIAL ANALYSIS OF THE GOVERNMENTAL ACTIVITIES (CONTINUED)

<u>Summary of Revenues For Governmental Functions</u>				
	FYE 2011 Amount	Percent of Total	FYE 2012 Amount	Percent of Total
<u>Program Revenues</u>				
Charges for Services	\$ 817,028	1.06%	\$ 876,740	1.15%
Operating Grants & Contributions *	12,349,250	16.09%	13,435,755	17.58%
Capital Grants & Contributions	3,059	0.00%	485	0.00%
<u>General Revenues</u>				
Taxes Levied	33,063,803	43.09%	33,458,364	43.79%
Federal & State Aid *	27,055,040	35.26%	24,568,424	32.16%
Other Revenues	3,444,172	4.49%	4,066,244	5.32%
Total Revenues	\$ 76,732,352	100.00%	\$ 76,406,012	100.00%

Table includes financial data of the combined governmental funds

* Prior year balances have been adjusted to reflect the restatement discussed at Note 22 in these financial statements.



**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

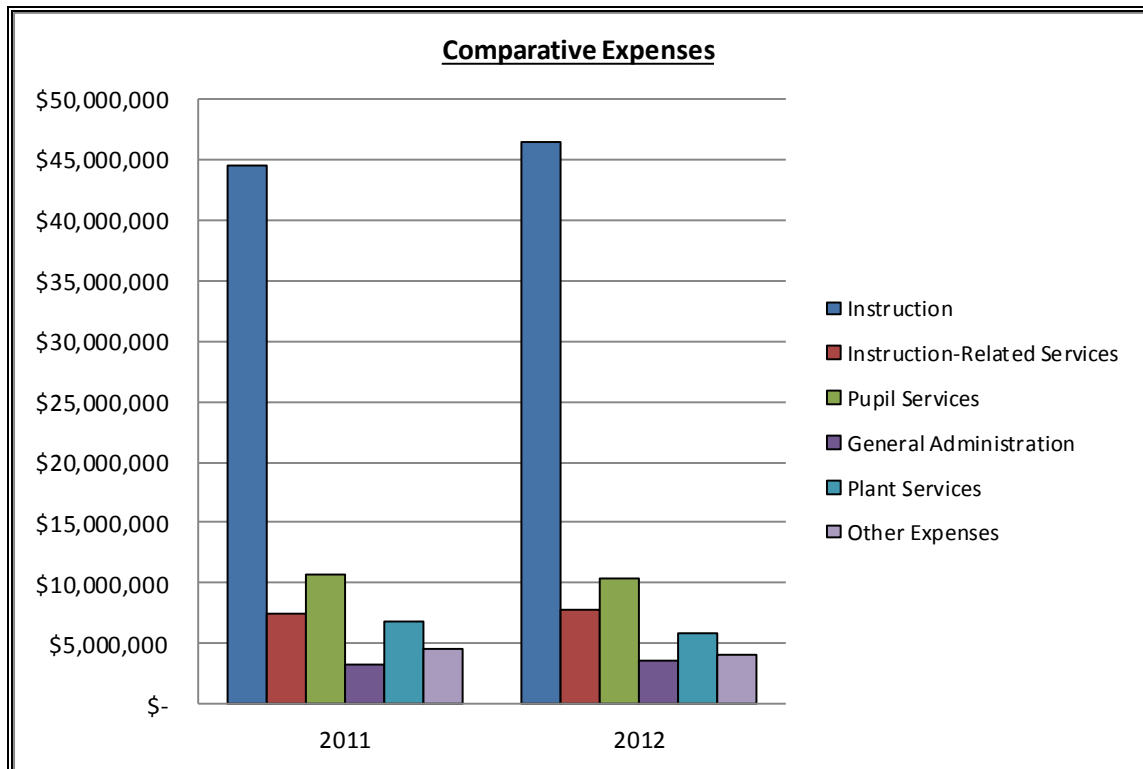
(PREPARED BY DISTRICT MANAGEMENT)

FINANCIAL ANALYSIS OF THE GOVERNMENTAL ACTIVITIES (CONCLUDED)

Schedule of Expenses For Governmental Functions

<u>Expenses</u>	<u>FYE 2011 Amount</u>	<u>Percent of Total</u>	<u>FYE 2012 Amount</u>	<u>Percent of Total</u>
Instruction	\$ 44,474,359	57.54%	\$ 46,486,554	59.50%
Instruction-Related Services	7,395,891	9.57%	7,709,482	9.87%
Pupil Services	10,755,071	13.92%	10,355,045	13.25%
General Administration	3,207,291	4.15%	3,552,516	4.55%
Plant Services	6,846,894	8.86%	5,915,960	7.57%
Other Expenses	4,609,238	5.96%	4,102,732	5.25%
Total Expenses	\$ 77,288,744	100.00%	\$ 78,122,289	100.00%

Table includes financial data of the combined governmental funds



**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

(PREPARED BY DISTRICT MANAGEMENT)

FINANCIAL ANALYSIS OF THE CAPITAL ASSETS & LONG-TERM LIABILITIES

Governmental Activities:

<u>Comparative Schedule of Capital Assets</u>		
	2011	2012
Land	\$ 4,266,886	\$ 4,266,886
Sites & Improvements	12,580,090	14,432,076
Buildings & Improvements	136,638,241	136,638,241
Furniture & Equipment	6,131,949	6,401,361
Work-in-Progress	<u>506,298</u>	<u>772,232</u>
Totals at Historical Cost	160,123,464	162,510,796
Less: Accumulated Depreciation	<u>(56,337,528)</u>	<u>(61,490,823)</u>
Capital Assets, net	<u>\$ 103,785,936</u>	<u>\$ 101,019,973</u>

Capital assets, net of depreciation, decreased \$2,765,963, due to the current year addition of \$2,387,332 of new capital assets, and the current year recognition of \$5,153,295 of depreciation expense.

<u>Comparative Schedule of Long-Term Liabilities</u>		
	2011	2012
Compensated Absences	\$ 453,628	\$ 508,140
General Obligation Bonds *	58,871,742	55,951,530
Certificates of Participation	7,485,000	7,205,000
Capital Leases	3,482,034	3,202,925
Early Retirement Incentives	0	409,254
Other Post Employment Benefits	<u>300,843</u>	<u>230,824</u>
Totals *	<u>\$ 70,593,247</u>	<u>\$ 67,507,673</u>

* Prior year balances have been adjusted to reflect the restatement discussed at Note 22 in these financial statements.

Total long-term liabilities decreased \$3,085,574, due primarily to the current year reduction of the District's liabilities related to general obligation bonds.

The general obligation bonds are financed by the local taxpayers and represent 83% of the District's total long-term liabilities.

The notes to the financial statements are an integral part of the financial presentation and contain more detailed information as to the future debt service requirements of each long-term obligation.

**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

(PREPARED BY DISTRICT MANAGEMENT)

FINANCIAL ANALYSIS OF THE SCHOOL DISTRICT'S FUNDS

<u>Comparative Schedule of Fund Balances</u>			
	Fund Balances June 30, 2011	Fund Balances June 30, 2012	Increase (Decrease)
General *	\$ 12,716,860	\$ 12,435,459	\$ (281,401)
Bond Interest & Redemption	5,250,155	5,306,302	56,147
Deferred Maintenance *	1,060,027	942,787	(117,240)
Cafeteria	195,394	150,527	(44,867)
Adult Education *	410,693	325,074	(85,619)
Capital Facilities	521,558	908,776	387,218
Building	327,942	307,767	(20,175)
County School Facilities	158,358	80,250	(78,108)
Capital Projects - Special Reserve	1,057,489	722,743	(334,746)
Totals *	\$ 21,698,476	\$ 21,179,685	\$ (518,791)

* Prior year balances have been adjusted to reflect the reclassification and restatement discussed at Notes 20 & 21 in these financial statements.

The fund balance of the General Fund decreased \$281,401, while the combined fund balances of all other District governmental funds decreased \$237,390.

GENERAL FUND BUDGETARY HIGHLIGHTS

The District's budget is prepared in accordance with California law and is based on the modified accrual basis of accounting. The original budget, approved at the end of June, is based on May Revise figures and updated 45 days after the State approves its final budget. Over the course of the year, the District revised the annual operating budget on numerous occasions. The significant budget adjustments fell into the following categories:

- ◆ Budget revisions to the adopted budget required after approval of the State budget.
- ◆ Budget revisions to update revenues to actual enrollment information and to update expenditures for staffing adjustments related to actual enrollments.
- ◆ Adjustments at First and Second Interim.
- ◆ Other budget revisions are routine in nature, including adjustments to categorical revenues and expenditures based on final awards, and adjustments between expenditure categories for school and department budgets.

ECONOMIC FACTORS BEARING ON THE DISTRICT'S FUTURE

Student enrollment and attendance are primary factors in the computation of most funding formulas for public schools in the State of California. The District's fiscal year 2012-13 budget includes a projected increase of 58 ADA.

**PETALUMA CITY SCHOOLS
MANAGEMENT'S DISCUSSION AND ANALYSIS (UNAUDITED)
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

(PREPARED BY DISTRICT MANAGEMENT)

ECONOMIC FACTORS BEARING ON THE DISTRICT'S FUTURE (CONCLUDED)

On August 9, 2012, the District issued \$12,845,000 of general obligation refunding bonds for purposes of refunding \$12,775,000 of the District's outstanding 2005 General Obligation Refunding Bonds, maturing on and after August 1, 2013, and to pay costs of issuance of the Bonds. The refunding bonds were issued to take advantage of the current lower interest rates, which will ultimately result in a decreased tax burden for the individuals who own property within the District.

Due to the unprecedented nature of the current State and Federal fiscal crisis, the amount of funding that will be available to the District remains uncertain. As a result, management will need to plan carefully and prudently to provide the resources to meet student needs over the next several years. The District has an excellent track record in meeting this challenge in what has proven to be a cycle of lean years and prosperous years for education finances.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, parents, investors, and creditors with a general overview of the District's finances and to show the District's accountability for the money it receives. If you have questions regarding this report or need additional financial information, contact the Chief Business Official, Petaluma City Schools, 200 Douglas Street, Petaluma, CA 94952.

PETALUMA CITY SCHOOLS
STATEMENT OF NET ASSETS
JUNE 30, 2012

	Governmental Activities	Business-Type Activities	Totals
<u>Assets</u>			
Deposits and Investments (Note 2)	\$ 9,948,890	\$ 12,995	\$ 9,961,885
Receivables (Note 4)	16,157,165	1,020	16,158,185
Stores Inventory (Note 11)	59,265		59,265
Prepaid Expenses (Note 11)	1,473,160		1,473,160
Capital Assets: (Note 6)			
Land	4,266,886		4,266,886
Sites and Improvements	14,432,076		14,432,076
Buildings and Improvements	136,638,241		136,638,241
Furniture and Equipment	6,401,361	56,833	6,458,194
Work-in-Progress	772,232		772,232
Less: Accumulated Depreciation	(61,490,823)	(32,679)	(61,523,502)
Total Assets	<u>128,658,453</u>	<u>38,169</u>	<u>128,696,622</u>
<u>Liabilities</u>			
Accounts Payable and Other Current Liabilities	4,980,189	3,366	4,983,555
Deferred Revenue (Note 11)	528,486		528,486
Long-Term Liabilities:			
<i>Portion Due or Payable Within One Year:</i>			
Compensated Absences	508,140		508,140
General Obligation Bonds			
Current Interest	2,495,000		2,495,000
Capital Appreciation	1,368,636		1,368,636
Unamortized Bond Premium	60,640		60,640
Certificates of Participation	290,000		290,000
Capital Leases	246,546		246,546
Early Retirement Incentives	204,627		204,627
Other Post Employment Benefits	73,140		73,140
<i>Portion Due or Payable After One Year:</i>			
General Obligation Bonds (Note 7)			
Current Interest	38,485,000		38,485,000
Capital Appreciation	12,858,092		12,858,092
Unamortized Bond Premium	684,162		684,162
Certificates of Participation (Note 9)	6,915,000		6,915,000
Capital Leases (Note 10)	2,956,379		2,956,379
Early Retirement Incentives (Note 11)	204,627		204,627
Other Post Employment Benefits (Note 12)	157,684		157,684
Total Liabilities	<u>73,016,348</u>	<u>3,366</u>	<u>73,019,714</u>
<u>Net Assets</u>			
Investment in Capital Assets, Net of Related Debt	45,072,293	24,154	45,096,447
Restricted:			
For Capital Projects	1,337,337		1,337,337
For Debt Service	(3,938,102)		(3,938,102)
For Educational Programs	1,673,360		1,673,360
For Other Purposes	210,367	10,649	221,016
Unrestricted	11,286,850		11,286,850
Total Net Assets	<u>\$ 55,642,105</u>	<u>\$ 34,803</u>	<u>\$ 55,676,908</u>

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS

**PETALUMA CITY SCHOOLS
STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

Functions	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	Totals
<u>Governmental Activities</u>							
Instruction	\$ 46,486,554	\$ 59,152	\$ 7,983,568	\$ 485	\$ (38,443,349)		\$ (38,443,349)
Instruction-Related Services:							
Supervision of Instruction	2,020,348	525	1,043,314		(976,509)		(976,509)
Instructional Library and Technology	979,703		26,453		(953,250)		(953,250)
School Site Administration	4,709,431		160,114		(4,549,317)		(4,549,317)
Pupil Services:							
Home-to-School Transportation	2,773,470	26,634	1,416,508		(1,330,328)		(1,330,328)
Food Services	1,993,467	744,074	1,157,011		(92,382)		(92,382)
Other Pupil Services	5,588,108	10,308	1,240,997		(4,336,803)		(4,336,803)
General Administration:							
Other General Administration	3,552,516	27,204	144,296		(3,381,016)		(3,381,016)
Plant Services	5,915,960	3,328	204,377		(5,708,255)		(5,708,255)
Ancillary Services	326,689				(326,689)		(326,689)
Community Services	320,804				(320,804)		(320,804)
Enterprise Activities	407,367				(407,367)		(407,367)
Interest on Long-Term Debt	2,803,336				(2,803,336)		(2,803,336)
Other Outgo	244,536	5,515	59,117		(179,904)		(179,904)
Total Governmental Activities	78,122,289	876,740	13,435,755	485	(63,809,309)		(63,809,309)
<u>Business-Type Activities</u>							
Enterprise Activities	18,909	6,480				\$ (12,429)	(12,429)
Totals	\$ 78,141,198	\$ 883,220	\$ 13,435,755	\$ 485	(63,809,309)	(12,429)	(63,821,738)
<u>General Revenues</u>							
Taxes Levied for General Purposes					26,072,024		26,072,024
Taxes Levied for Debt Service					5,409,479		5,409,479
Taxes Levied for Specific Purposes					1,976,861		1,976,861
Federal and State Aid - Unrestricted					24,568,424		24,568,424
Interest and Investment Earnings					195,455	107	195,562
Miscellaneous					3,870,789		3,870,789
Total General Revenues					62,093,032	107	62,093,139
<u>Special Item</u>							
Donated Capital Improvements					1,283,263		1,283,263
Change in Net Assets					(433,014)	(12,322)	(445,336)
Net Assets - July 1, 2011 (As Restated - Note 22)					56,075,119	47,125	56,122,244
Net Assets - June 30, 2012					\$ 55,642,105	\$ 34,803	\$ 55,676,908

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS

**PETALUMA CITY SCHOOLS
BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2012**

	<u>General</u>	<u>Bond Interest and Redemption</u>	<u>Non-Major Governmental Funds</u>	<u>Total Governmental Funds</u>
<u>Assets</u>				
Deposits and Investments (Note 2)	\$ 2,014,065	\$ 5,306,302	\$ 2,624,673	\$ 9,945,040
Receivables (Note 4)	15,520,462		636,703	16,157,165
Due from Other Funds (Note 5)	5,953,168		3,928,098	9,881,266
Stores Inventory (Note 11)	37,771		21,494	59,265
Total Assets	<u>\$ 23,525,466</u>	<u>\$ 5,306,302</u>	<u>\$ 7,210,968</u>	<u>\$ 36,042,736</u>
<u>Liabilities and Fund Balances</u>				
Liabilities:				
Accounts Payable	\$ 3,872,865		\$ 488,614	\$ 4,361,479
Due to Other Funds (Note 5)	6,709,949		3,263,137	9,973,086
Deferred Revenue (Note 11)	507,193		21,293	528,486
Total Liabilities	<u>11,090,007</u>		<u>3,773,044</u>	<u>14,863,051</u>
Fund Balances: (Note 14)				
Nonspendable	57,771		21,944	79,715
Restricted	1,673,360	\$ 5,306,302	1,775,756	8,755,418
Assigned	930,298		1,640,224	2,570,522
Unassigned	9,774,030			9,774,030
Total Fund Balances	<u>12,435,459</u>	<u>5,306,302</u>	<u>3,437,924</u>	<u>21,179,685</u>
Total Liabilities and Fund Balances	<u>\$ 23,525,466</u>	<u>\$ 5,306,302</u>	<u>\$ 7,210,968</u>	<u>\$ 36,042,736</u>

PETALUMA CITY SCHOOLS
RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO
THE STATEMENT OF NET ASSETS
JUNE 30, 2012

Total Fund Balances - Governmental Funds \$ 21,179,685

Amounts reported for governmental activities in the statement of net assets are different due to the following:

Capital assets used in governmental activities are not financial resources and therefore are not reported as assets in governmental funds. The amount that capital assets exceeded accumulated depreciation was:

Capital Assets	\$ 162,510,796	
Accumulated Depreciation	(61,490,823)	
		101,019,973

Unamortized costs: In governmental funds, debt issuance costs are recognized as expenditures in the period they are incurred. In the government-wide statements, debt issuance costs are amortized over the life of the debt. Unamortized debt issue costs, reported as prepaid expenses at year-end consist of:

Prepaid Expense - Costs of Issuance	\$ 521,420	
Prepaid Expense - Refunding	951,740	
		1,473,160

The assets and liabilities of the internal service fund are not included in the governmental fund statements, but are included in the governmental activities. The net assets of the District's self-insurance fund were:

90,516

Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported as liabilities in the governmental funds. Long-term liabilities at year-end was:

Compensated Absences	\$ 508,140	
General Obligation Bonds		
Current Interest Bonds	40,980,000	
Capital Appreciation Bonds	14,226,728	
Unamortized Bond Premium	744,802	
Certificates of Participation	7,205,000	
Capital Leases	3,202,925	
Early Retirement Incentives	409,254	
Other Post Employment Benefits	230,824	
		(67,507,673)

In governmental funds, the unmatured interest on long-term debt is not recognized until the period in which it matures and is paid. In the government-wide statements of activities, it is recognized in the period that it is incurred. The liability for unmatured interest owed at the end of the period was:

(613,556)

Total Net Assets - Governmental Activities \$ 55,642,105

PETALUMA CITY SCHOOLS
STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	<u>General</u>	<u>Bond Interest and Redemption</u>	<u>Non-Major Governmental Funds</u>	<u>Total Governmental Funds</u>
<u>Revenues</u>				
Revenue Limit Sources:				
State Apportionment	\$ 16,055,211			\$ 16,055,211
Local Taxes	26,072,024			26,072,024
Total Revenue Limit Sources	42,127,235			42,127,235
Federal Revenue	5,609,532		\$ 1,173,164	6,782,696
State Revenue	10,276,182	\$ 49,484	1,250,575	11,576,241
Local Revenue	8,172,764	5,397,630	2,350,705	15,921,099
Total Revenues	66,185,713	5,447,114	4,774,444	76,407,271
<u>Expenditures</u>				
Instruction	41,599,428		884,486	42,483,914
Supervision of Instruction	1,924,406			1,924,406
Instructional Library and Technology	784,859			784,859
School Site Administration	4,380,782		271,183	4,651,965
Home-To-School Transportation	2,767,650			2,767,650
Food Services			1,952,744	1,952,744
Other Pupil Services	5,521,264		65,299	5,586,563
Other General Administration	2,548,255		131,309	2,679,564
Plant Services	5,443,178		798,570	6,241,748
Facilities Acquisition and Construction			544,812	544,812
Ancillary Services	300,699			300,699
Community Services	305,153			305,153
Enterprise Activities	357,393			357,393
Debt Service:				
Principal Retirement	298,548	12,553,791	284,434	13,136,773
Interest and Issuance Costs	203,037	1,759,605	135,144	2,097,786
Other Outgo	56,335			56,335
Total Expenditures	66,490,987	14,313,396	5,067,981	85,872,364
Excess of Revenues				
(Under) Expenditures	(305,274)	(8,866,282)	(293,537)	(9,465,093)
<u>Other Financing Sources</u>				
Other Sources	23,873	8,922,429		8,946,302
Net Change in Fund Balances	(281,401)	56,147	(293,537)	(518,791)
Fund Balances - July 1, 2011 (As Reclassified / Restated - Notes 20 & 21)	12,716,860	5,250,155	3,731,461	21,698,476
Fund Balances - June 30, 2012	\$ 12,435,459	\$ 5,306,302	\$ 3,437,924	\$ 21,179,685

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS

PETALUMA CITY SCHOOLS
RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES,
AND CHANGES IN FUND BALANCES TO THE STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

Net Change in Fund Balances - Governmental Funds	\$ (518,791)
Amounts reported for governmental activities in the statement of activities are different due to the following:	
Capital outlays to purchase or build capital assets are reported in governmental funds as expenditures. However, for governmental activities those costs are shown in the statement allocated over their estimated useful lives as annual depreciation expenses in the statement of activities. This is the amount by which depreciation expense exceeded capital outlays during the fiscal year:	(4,049,226)
Donated capital assets: In governmental funds, donated capital assets are not reported because they do not affect current financial resources. In the government-wide statements, donated capital assets are reported as revenue and as increases to capital assets, at their fair market value on the date of donation. The fair market value of capital assets donated was:	1,283,263
Earned but unavailable revenues: In governmental funds, revenues are recognized only to the extent that they are "available," meaning they will be collected soon enough after the end of the period to finance expenditures of that period. In the government-wide statements, revenue is recognized when earned, regardless of availability. The amount of earned but unavailable revenues relating to the current period, less revenues that became available in the current period but related to a prior period, is:	(62,493)
Debt proceeds: In governmental funds, proceeds from debt are recognized as Other Financing Sources. In the government-wide statements, proceeds from debt are reported as increases to liabilities. Amounts recognized in governmental funds as proceeds from debt were:	(8,946,302)
Bond refunding cost and debt issue costs are recognized as expenditures in the period they are incurred in governmental funds. In the government-wide statements, these costs are amortized over the life of the debt. The difference between bond refunding and debt issue costs recognized in the current period, and bond refunding and debt issue costs amortized for the current period are:	
Bond Refunding	\$ 124,987
Cost of Issuance	102,443
Cost of Issuance Amortized	(188,201)
Bond Refunding Amortized	(360,757)
	(321,528)
In the statement of activities, certain operating expenses-compensated absences (vacations) are measured by the amounts earned during the fiscal year. In the governmental funds, however, expenditures for this type of expenditure is measured by the amount of financial resources used (essentially, the amounts actually paid). During the current year, compensated absences used exceeded compensated absences earned by:	(54,512)
Postemployment benefits other than pensions (OPEB): In governmental funds, OPEB costs are recognized when employer contributions are made. In the statement of activities, OPEB costs are recognized on the accrual basis. This year, the difference between OPEB costs and actual employer contributions was:	70,019
Early retirement incentives: Early retirement incentives costs are recognized when employer contributions are made. In the statement of activities, early retirement incentives costs are recognized on the accrual basis. This year, the difference between early retirement incentives costs and actual employer contributions was:	(409,254)
Debt Service: In the governmental funds, repayment of long-term obligations are reported as expenditures. In the government-wide statements, repayments of long-term obligations are reported as reduction of liabilities. The amount of expenditures made for the repayment of the principal portion of long-term obligations during the year was:	
General Obligation Bonds	
Current Interest Bonds	\$ 11,178,791
Capital Appreciation Bonds	1,375,000
Unamortized Bond Premium	43,910
Certificates of Participation	280,000
Capital Leases	302,982
	13,180,683
Accreted interest on capital appreciation bonds is not recognized as an expenditure in the governmental fund financial statements until paid. In the statement of activities, however, accreted interest is recognized as an expense as the capital appreciation bonds accrete in value. The amount of accreted interest recognized in the current year is:	(755,060)
Interest on long-term debt in the statement of activities differs from the amount reported in the governmental funds because interest is recorded as an expenditure in the funds when it is due, and thus requires the use of current financial resources. In the statement of activities, however, interest expense is recognized as the interest accrues, regardless of when it is due. Accrued interest on outstanding general obligation bonds, certificates of participation, and capital leases increased by:	138,927
The income and expense of internal service funds are not included in the governmental fund statements, but are included in the governmental activities. The amount that income exceeded expense during the year was:	11,260
Change in Net Assets of Governmental Activities	\$ (433,014)

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS

**PETALUMA CITY SCHOOLS
STATEMENT OF NET ASSETS
PROPRIETARY FUNDS
JUNE 30, 2012**

	Governmental Activities	Business-Type Activities
	Internal Service	Enterprise
	Self-Insurance Fund	Downtown Project Fund
<u>Assets</u>		
Deposits and Investments (Note 2)	\$ 3,850	\$ 12,995
Receivables (Note 4)		1,020
Due from Other Funds (Note 5)	91,820	
Capital Assets: (Note 6)		
Furniture and Equipment		56,833
Less: Accumulated Depreciation		(32,679)
Total Assets	<u>95,670</u>	<u>38,169</u>
<u>Liabilities</u>		
Accounts Payable	<u>5,154</u>	<u>3,366</u>
Total Liabilities	<u>5,154</u>	<u>3,366</u>
<u>Net Assets</u>		
Investment in Capital Assets		24,154
Restricted	90,516	
Assigned		<u>10,649</u>
Total Net Assets	<u><u>\$ 90,516</u></u>	<u><u>\$ 34,803</u></u>

PETALUMA CITY SCHOOLS
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
PROPRIETARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	Governmental Activities	Business-Type Activities
	Internal Service	Enterprise
	Self-Insurance Fund	Downtown Project Fund
<u>Operating Revenues</u>		
Local Revenue	\$ 61,069	\$ 6,480
Total Operating Revenues	61,069	6,480
<u>Operating Expenses</u>		
Books and Supplies		11,384
Contract Services	49,974	1,838
Depreciation		5,687
Total Operating Expenses	49,974	18,909
Operating Income (Loss)	11,095	(12,429)
<u>Non-Operating Revenues</u>		
Interest	165	107
Change in Net Assets	11,260	(12,322)
Net Assets - July 1, 2011	79,256	47,125
Net Assets - June 30, 2012	\$ 90,516	\$ 34,803

**PETALUMA CITY SCHOOLS
STATEMENT OF CASH FLOWS
PROPRIETARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

	Governmental Activities	Business-Type Activities
	Internal Service	Enterprise
	Self-Insurance Fund	Downtown Project Fund
<i>Cash Flows From Operating Activities:</i>		
Cash Received from Services	\$ 12,050	\$ 6,243
Payments to Suppliers for Goods and Services	(48,597)	(9,856)
Net Cash Provided (Used) by Operating Activities	(36,547)	(3,613)
<i>Cash Flows From Investing Activities:</i>		
Interest	165	107
Net Increase (Decrease) in Cash	(36,382)	(3,506)
Deposits and Investments - July 1, 2011	40,232	16,501
Deposits and Investments - June 30, 2012	\$ 3,850	\$ 12,995
<i>Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:</i>		
Operating Income (Loss)	\$ 11,095	\$ (12,429)
Adjustments to Reconcile Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:		
Depreciation		5,687
Changes in Operating Assets and Liabilities:		
Receivables	6,419	(237)
Due from Other Funds	(55,497)	
Accounts Payable	1,436	3,366
Net Cash Provided (Used by) Operating Activities	\$ (36,547)	\$ (3,613)

**PETALUMA CITY SCHOOLS
STATEMENT OF NET ASSETS
FIDUCIARY FUNDS
JUNE 30, 2012**

	Private-Purpose Trust	Agency	Total
	Scholarship Fund	Student Body Fund	Fiduciary Funds
<u>Assets</u>			
Deposits and Investments (Note 2)	\$ 102,235	\$ 491,728	\$ 593,963
Receivables	233		233
Total Assets	<u>102,468</u>	<u>491,728</u>	<u>594,196</u>
<u>Liabilities</u>			
Due to Student Groups		491,728	491,728
Accounts Payable	250		250
Total Liabilities	<u>250</u>	<u>491,728</u>	<u>491,978</u>
<u>Net Assets</u>			
Restricted	<u>102,218</u>	<u>0</u>	<u>102,218</u>
Total Net Assets	<u>\$ 102,218</u>	<u>\$ 0</u>	<u>\$ 102,218</u>

**PETALUMA CITY SCHOOLS
STATEMENT OF CHANGES IN NET ASSETS
FIDUCIARY FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

	Private-Purpose Trust
	Scholarship Fund
<u>Additions</u>	
Gifts and Contributions	\$ 1,505
Interest	1,883
Total Additions	3,388
<u>Deductions</u>	
Scholarships Awarded	12,778
Total Deductions	12,778
Change in Net Assets	(9,390)
<u>Net Assets</u>	
Net Assets - July 1, 2011	111,608
Net Assets - June 30, 2012	\$ 102,218

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

A. Financial Reporting Entity

These financial statements report the combined financial activities of the Petaluma City Elementary School District and the Petaluma Joint Union High School District. The districts share a common administration, and staff as permitted under Education Code Section 35110. These two entities are referred to collectively as Petaluma City Schools, and for purposes of these financial statement notes will be referred to collectively as the District.

The District is a public educational agency operating under the applicable laws and regulations of the State of California. It is governed by a five member Board of Education elected by registered voters of the District, which comprises an area in Sonoma County. The District was established in 1857 and serves students in kindergarten through grade twelve.

The District accounts for its financial transactions in accordance with the policies and procedures of the Department of Education's *California School Accounting Manual*. The accounting policies of the District conform to generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB) and the American Institute of Certified Public Accountants (AICPA).

The District has reviewed criteria to determine whether other organizations with activities that benefit the District should be included within its financial reporting entity under GASB Statement No. 14 (GASB 14), *The Financial Reporting Entity*. The criteria include, but are not limited to, whether the organization exercises oversight responsibility (which includes financial interdependency, selection of governing authority, designation of management, ability to significantly influence operations and accountability for fiscal matters), the scope of public service, and a special financing relationship. The District has determined that there are no organizations, with financial activities that benefit the District, which should be included within its financial reporting entity under GASB 14.

The District has also reviewed criteria to determine whether other organizations, for which the District is not financially accountable, should be reported within its financial reporting entity, based on the nature and significance of its relationship with the District, under GASB Statement No. 39 (GASB 39), *Determining Whether Certain Organizations are Component Units*. In order for an organization to be classified as a component unit, all of the GASB 39 criteria must be met, as follows:

- The economic resources received or held by the organization are entirely or almost entirely for the direct benefit of the primary government or its component units.
- The primary government, or its component units, is entitled to, or has the ability to otherwise access, a majority of the economic resources received or held by the organization.
- The economic resources received or held by the organization that the primary government, or its component units, is entitled to, or has the ability to otherwise access, are significant to that primary government.

The District has determined that there are no organizations, for which the District is not financially accountable, which should be reported within its financial reporting entity under GASB 39.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

B. Basis of Presentation

Government-wide Financial Statements:

The government-wide financial statements (i.e., the Statement of Net Assets and the Statement of Activities) report information on all of the nonfiduciary activities of the District and its component units. The effect of interfund activity, within the governmental and business-type activities columns, has been removed from these statements. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.

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

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. The District does not allocate indirect expenses to functions in the statement of activities. Program revenues include charges paid by the recipients of goods or services offered by a program, as well as grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues which are not classified as program revenues are presented as general revenues of the District, with certain exceptions. The comparison of direct expenses with program revenues identifies the extent to which each 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 governmental fund is presented in a separate column, and all non-major funds are aggregated into one column. The Enterprise Fund is presented on the proprietary fund statements. Fiduciary funds are reported by fund type.

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

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

B. Basis of Presentation (Concluded)

Fund Financial Statements (Concluded):

All proprietary fund types are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the proprietary fund's Statement of Net Assets. The Statement of Revenues, Expenses, and Changes in Net Assets for proprietary funds present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets. The Statement of Cash Flows provides information about how the District finances and meets the cash flow needs of its proprietary activities.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations.

Fiduciary funds are reported using the economic resources measurement focus.

C. Basis of Accounting

Basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in 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 use the accrual basis of accounting.

Revenues – Exchange and Non-exchange Transactions:

Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded under the accrual basis when the exchange takes place. Under the modified accrual basis, revenue is recorded in the fiscal year in which the resources are measurable and become available. "Available" means 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 collectible within the current period or within 45, 60, 90 days after year-end, depending on the revenue source. However, to achieve comparability of reporting among California Districts and so as not to distort normal revenue patterns, with specific respect to reimbursement grants and corrections to state aid apportionments, the California Department of Education has defined available as collectible within one year.

Non-exchange transactions, in which the District receives value without directly giving equal value in return, include property taxes, grants, and entitlements. Under the accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied.

Revenue from grants and entitlements 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 resources are 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 specific purpose; and expenditure requirements, in which the resources are provided to the District on a reimbursement basis. Under the modified accrual basis, revenue from non-exchange transactions must also be available before it can be recognized.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Basis of Accounting (Concluded)

Deferred Revenue:

Deferred revenue arises when assets are received before revenue recognition criteria have been satisfied. Grants and entitlements received before eligibility requirements are met are recorded as deferred revenue. On governmental fund financial statements, receivables associated with non-exchange transactions that will not be collected within the availability period have also been recorded as deferred revenue.

Expenses/Expenditures:

On an accrual basis of accounting, expenses are recognized at the time a liability is incurred. On the modified accrual basis of accounting, expenditures are generally recognized in the accounting period in which the related fund liability is incurred, as under the accrual basis of accounting. However under the modified accrual basis of accounting, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due. Allocations of cost, such as depreciation and amortization, are not recognized in the governmental funds.

When both restricted and unrestricted resources are available for use, it is the District's policy to use restricted resources first, then unrestricted resources as they are needed.

D. Fund Accounting

The accounts of the District are organized on the basis of funds, each of which is considered to be a separate accounting entity. The operations of each fund are accounted for with a separate set of self-balancing accounts that comprise its assets, liabilities, fund equity or retained earnings, revenues, and expenditures or expenses, as appropriate. District resources are allocated to and accounted for in individual funds based upon the purpose for which they are to be spent and the means by which spending activities are controlled. The District maintains the following fund types:

General Fund - The general fund is used to account for and report all financial resources not accounted for and reported in another fund.

Special Revenue Funds - Special revenue funds are used to account for and report the proceeds of specific revenue sources that are restricted or committed to expenditure for specified purposes other than debt service or capital projects. Other resources also may be reported in the fund if those resources are restricted, committed, or assigned to the specified purpose of the fund.

Debt Service Funds - Debt service funds are used to account for and report financial resources that are restricted, committed, or assigned to expenditure for principal and interest.

Capital Projects Funds - Capital projects funds are used to account for and report financial resources that are restricted, committed, or assigned to expenditure for capital outlays, including the acquisition or construction of capital facilities and other capital assets.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

D. Fund Accounting (Continued)

Proprietary Funds - Proprietary funds focus on the determination of the changes in net assets, financial position and cash flows and are classified as either enterprise or internal service.

Fiduciary Funds - Fiduciary funds are classified as either *Private-Purpose Trust Funds*, which are used to account for assets held by the District as trustee, or *Agency Funds*, which are used to account for assets of others for which the District acts as an agent.

The District's accounts are organized into major, non-major, proprietary, and fiduciary funds as follows:

Major Governmental Funds:

General Fund is the general operating fund of the District. It is used to account for and report all financial resources not accounted for and reported in another fund.

Bond Interest and Redemption Fund is used to account for District taxes received and expended to pay bond interest and redeem bond principal and related costs.

Non-major Governmental Funds:

Deferred Maintenance Fund is used for the purpose of major repair or replacement of District property.

Cafeteria Fund is used to account for revenues received and expenditures made to operate the District's cafeteria program.

Adult Education Fund is used to account for resources committed to adult education programs maintained by the District.

Capital Facilities Fund is used to account for resources received from developer impact fees assessed under provision of the California Environmental Quality Act (CEQA).

Building Fund is used to account for proceeds from sale of bonds (Education Code Section 15146), which may not be used for any purpose other than those for which the bonds were issued.

County School Facilities Fund is used to account for state apportionments (Education Code Sections 17009.5 and 17070.10-17076.10).

Capital Projects - Special Reserve Fund is used to provide for the accumulation of General Fund monies for Capital Outlay purposes (Education Code Section 42840).

Proprietary Fund:

Down Town Project Fund is an enterprise fund that was established to account for transactions of the Downtown Project, which are financed and operated in a manner similar to a business enterprise, where the intent is to recover the cost of providing the services through user charges.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

D. Fund Accounting (Concluded)

Proprietary Fund:

Self-Insurance Fund is an internal service funds that was established to account for any activity for which services are provided to other funds of the District on a cost reimbursement basis.

Fiduciary Funds:

Scholarship Fund is a private-purpose trust fund, which is used to account for assets held by the District as trustee. The Scholarship Fund consists of the Schwobeda Memorial Trust Fund and the At Risk Youth Trust Fund, which are both used to provide financial assistance to students of the District.

Student Body Fund is an agency that is used to account for assets of others for which the District acts as an agent. The District maintains a Student Body Fund to account for the student body accounts at each school site, which are used to account for the raising and expending of money to promote the general welfare, and educational experience of the student body.

E. Budgets and Budgetary Accounting

Annual budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America for all governmental funds. By state law, the District's Governing Board must adopt a final budget no later than July 1. A public hearing must be conducted to receive comments prior to adoption. The District's Governing Board satisfied these requirements.

These budgets are revised by the District's Governing Board and Superintendent during the year to give consideration to unanticipated income and expenditures. The original and final revised budgets are presented for the General Fund as required supplementary information on page 53.

Formal budgetary integration was employed as a management control device during the year for all budgeted funds. The District employs budget control by minor object and by individual appropriation accounts. Expenditures cannot legally exceed appropriations by major object account (See Note 3).

F. 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 certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

G. Encumbrances

Encumbrance accounting is used in all budgeted funds to reserve portions of applicable appropriations for which commitments have been made. Encumbrances are recorded for purchase orders, contracts, and other commitments when they are written. Encumbrances are liquidated when the commitments are paid. All encumbrances are liquidated at June 30.

H. Cash and Cash Equivalents

For purposes of the Statement of Cash Flows for the District's proprietary fund, the District considers all highly liquid investment instruments (including restricted assets) purchased with a maturity of three months or less to be cash equivalents.

I. Assets, Liabilities and Equity

1. Deposits and Investments

The District is authorized to maintain cash in banks and revolving funds that are insured to \$250,000 by the Federal Depository Insurance Corporation (FDIC).

The District is considered to be an involuntary participant in an external investment pool as the District is required to deposit all receipts and collections of monies with their County Treasurer (Education Code Section 41001). The County is authorized to deposit cash and invest excess funds by California *Government Code* Section 53648 et seq. The funds maintained by the County are either secured by the FDIC or are collateralized.

The District is authorized under California Government Code to make direct investments in local agency bonds, notes, or warrants within the State; U.S. Treasury instruments; registered State warrants or treasury notes; securities of the U.S. Government, or its agencies; bankers acceptances; commercial paper; certificates of deposit placed with commercial banks and/or savings and loan companies; repurchase or reverse repurchase agreements; medium term corporate notes; shares of beneficial interest issued by diversified management companies; certificates of participation; obligations with first priority security; and collateralized mortgage obligations.

Investments with original maturities greater than one year are stated at fair value. Fair value is estimated based on quoted market prices at year-end. All investments not required to be reported at fair value are stated at cost or amortized cost.

2. Stores Inventory and Prepaid Expenses

Inventories are recorded using the consumption method in that inventory acquisitions are initially recorded in inventory asset accounts and are recorded as expenditures when the supplies are used. Inventories are valued at average cost and consist of expendable supplies held for consumption.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

I. Assets, Liabilities and Equity (Continued)

2. Stores Inventory and Prepaid Expenses (Concluded)

Reported inventories are equally offset by a net assets reserve, which indicates that these amounts are not "available for appropriation and expenditure" even though they are a component of net current assets.

Prepaid expenses include issuance costs and refunding costs related to prior year and current year debt issues, which are being amortized over the life of the obligations. Reported prepaid expenses are equally offset by a net assets reserve, which indicates that these amounts are not "available for appropriation and expenditure" even though they are a component of net current assets.

3. Capital Assets

Furniture and equipment purchased or acquired with an original cost of \$5,000 or more, and capital improvement, acquisition, or construction with an original cost of \$50,000 or more, are reported at historical cost or estimated historical cost. Contributed assets are reported at fair market value as of the date received. Additions, improvements, and other capital outlays that significantly extend the useful life of an asset are capitalized. The costs of normal maintenance and repairs that do not add to the value of the assets or materially extend the asset's lives are not capitalized, but are expensed as incurred. Depreciation on all capital assets is computed using a straight-line basis over the following estimated useful lives:

<u>Asset Class</u>	<u>Years</u>
Sites and Improvements	10-15
Buildings and Improvements	25-40
Furniture and Equipment	5-15

4. Deferred Revenue

Cash received for federal and state special projects and programs is recognized as revenue to the extent that qualified expenditures have been incurred. Deferred revenue is recorded to the extent that cash received on specific projects and programs exceeds qualified expenditures.

5. Compensated Absences

All vacation pay and labor related benefits are accrued when incurred in the government-wide financial statements.

Accumulated sick leave benefits are not recognized as liabilities of the District. The District's policy is to record sick leave as an operating expense in the period taken, since such benefits do not vest, nor is payment probable; however, unused sick leave is added to the creditable service period for calculation of retirement benefits when the employee retires.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

I. Assets, Liabilities and Equity (Continued)

6. Long-term Liabilities

In the government-wide financial statements, long-term obligations are reported as liabilities in the Statement of Net Assets. Premiums and discounts, as well as issuance costs, related to long-term obligations issued after the implementation of GASB Statement No. 34, are deferred and amortized over the life of the obligation when material to the financial statements. Long-term liabilities are reported net of the applicable premiums, discounts and issuance costs.

In the fund financial statements, governmental funds recognize the face amount of the obligation, including premiums, discounts as well as issuance costs, during the current period. The face amount of the obligations, premiums, discounts, or issuance costs is reported as other financing sources or uses.

7. Fund Balance Classification

The governmental fund financial statements present fund balances based on classifications that comprise a hierarchy that is based primarily on the extent to which the District is bound to honor constraints on the specific purposes for which amounts in the respective governmental funds can be spent. The classifications used in the governmental fund financial statements are as follows:

Nonspendable Fund Balance consists of funds that cannot be spent due to their form (e.g. inventories and prepaids) or funds that legally or contractually must be maintained intact.

Restricted Fund Balance consists of funds that are mandated for a specific purpose by external parties, constitutional provisions or enabling legislation.

Committed Fund Balance consists of funds that are set aside for a specific purpose by the district's highest level of decision making authority (governing board). Formal action must be taken prior to the end of the fiscal year. The same formal action must be taken to remove or change the limitations placed on the funds.

Assigned Fund Balance consists of funds that are set aside with the intent to be used for a specific purpose by the district's highest level of decision making authority or a body or official that has been given the authority to assign funds. In accordance with board policy, only the governing board and the Chief Business Official / Assistant Superintendent of Business Services may assign amounts for specific purposes.

Unassigned Fund Balance consists of excess funds that have not been classified in the previous four categories. All funds in this category are considered spendable resources. This category also provides the resources necessary to meet unexpected expenditures and revenue shortfalls. In accordance with board policy, the District intends to maintain a Reserve for Economic Uncertainties of at least 3% of the General Fund's annual total expenditures and other financing uses.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES (CONCLUDED)

I. Assets, Liabilities and Equity (Concluded)

7. Fund Balance Classification (Concluded)

The District considers restricted fund balances to have been spent first when an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available. Similarly, when an expenditure is incurred for purposes for which amounts in any of the unrestricted classifications of fund balance could be used, the District considers committed amounts to be reduced first, followed by assigned amounts and then unassigned amounts.

8. Revenue Limit/Property Tax

The District's revenue limit is received from a combination of local property taxes, state apportionments, and other local sources.

The County of Sonoma is responsible for assessing, collecting and apportioning property taxes. Taxes are levied for each fiscal year on taxable real and personal property in the county. The levy is based on the assessed values as of the preceding January 1, which is also the lien date. Property taxes on the secured roll are due on November 1 and February 1, and taxes become delinquent after December 10 and April 10, respectively. Property taxes on the unsecured roll are due on the lien date (January 1), and become delinquent if unpaid by August 31.

Secured property taxes are recorded as revenue when apportioned, in the fiscal year of the levy. The county apportions secured property tax revenue in accordance with the alternative method of distribution prescribed by Section 4705 of the California *Revenue and Taxation Code*. This alternate method provides for crediting each applicable fund with its total secured taxes upon completion of the secured tax roll, approximately October 1 of each year.

The County Auditor reports the amount of the District's allocated property tax revenue to the California Department of Education. Property taxes are recorded as local revenue limit sources by the District. The California Department of Education reduces the District's entitlement by the District's local property tax revenue. The balance is paid from the State General Fund, and is known as the State Apportionment.

The District's Base Revenue Limit is the amount of general purpose tax revenue, per average daily attendance (ADA), that the District is entitled to by law. This amount is multiplied by the second period ADA to derive the District's total entitlement.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 2 - DEPOSITS AND INVESTMENTS

Summary of Deposits and Investments

Deposits and investments as of June 30, 2012, consist of the following:

	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Fiduciary Activities</u>
Cash on Hand and in Banks	\$ 2,000		\$ 593,946
Cash in Revolving Fund	20,450		
Cash with Fiscal Agent	348,311		
County Pool Investments	<u>9,578,129</u>	<u>\$ 12,995</u>	<u>17</u>
Total Deposits and Investments	<u>\$ 9,948,890</u>	<u>\$ 12,995</u>	<u>\$ 593,963</u>

Cash on Hand and in Banks

Cash on hand and in banks consists of all cash held by the District and all cash maintained in commercial bank accounts owned by the District, exclusive of amounts held in revolving funds.

Cash in Revolving Fund

Cash in revolving fund consists of all cash maintained in commercial bank accounts that are used as revolving funds.

Cash with Fiscal Agent

Cash with fiscal agent consists of \$348,311 held by Zions First National Bank as trustee for the outstanding Alameda Contra-Costa Schools Financing Authority Variable Rate Demand Certificates of Participation, 2010 Series N.

County Pool Investments

County pool investments consist of District cash held by the Sonoma County Treasury that is invested in the county investment pool. The fair value of the District's investment in the pool is reported in the financial statements at amounts that are based upon the District's pro-rata share of the fair value provided by the County Treasurer for the entire portfolio (in relation to the amortized cost of that portfolio).

General Authorization

Limitations as they relate to interest rate risk, credit risk, and concentration of credit risk are indicated in the schedule below:

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 2 - DEPOSITS AND INVESTMENTS (CONTINUED)

General Authorization (Concluded)

Authorized Investment Type	Maximum Remaining Maturity	Maximum Percentage of Portfolio	Maximum Investment in One Issuer
Local Agency Bonds, Notes, Warrants	5 years	None	None
Registered State Bonds, Notes, Warrants	5 years	None	None
U.S. Treasury Obligations	5 years	None	None
U.S. Agency Securities	5 years	None	None
Banker's Acceptance	180 days	40%	30%
Commercial Paper	270 days	25%	10%
Negotiable Certificates of Deposit	5 years	30%	None
Repurchase Agreements	1 year	None	None
Reverse Repurchase Agreements	92 days	20% of base	None
Medium-Term Notes	5 years	30%	None
Mutual Funds	N/A	20%	10%
Money Market Mutual Funds	N/A	20%	10%
Mortgage Pass-Through Securities	5 years	20%	None
County Pooled Investment Funds	N/A	None	None
Local Agency Investment Fund (LAIF)	N/A	None	None
Joint Powers Authority Pools	N/A	None	None

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rate will adversely affect the fair value of an investment. Generally, as the length of the maturity of an investment increases, the greater the sensitivity of its fair value to changes in market interest rates. The District manages its exposure to interest rate risk by investing in the County Treasury that purchases a combination of shorter term and longer term investments and by timing cash flows from maturities so that a portion of the portfolio is maturing or coming close to maturity evenly over time as necessary to provide the cash flow and liquidity needed for operations.

Segmented Time Distribution

Information about the sensitivity of the fair value of the District's investment to market interest rate fluctuations is provided by the following schedule that shows the distribution of the District's investment by maturity:

Governmental Activities:

Investment Type	Carrying Value	Fair Value	Less Than 1 Year	More Than 1 Year
County Pool Investments	\$ 9,578,129	\$ 9,592,592	\$ 2,730,052	\$ 6,848,077

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 2 - DEPOSITS AND INVESTMENTS (CONTINUED)

Segmented Time Distribution (Concluded)

Business-Type Activities:

<u>Investment Type</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Less Than 1 Year</u>	<u>More Than 1 Year</u>
County Pool Investments	\$ 12,995	\$ 13,015	\$ 3,704	\$ 9,291

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the minimum rating required by the California Government Code, the District's investment policy, or debt agreements, and the actual rating as of the year-end for each investment type.

Governmental Activities:

<u>Investment Type</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Rating as of Year End</u>		
			<u>AAA</u>	<u>Aa</u>	<u>Unrated</u>
County Pool Investments	\$ 9,578,129	\$ 9,592,592			\$ 9,578,129

Business-Type Activities:

<u>Investment Type</u>	<u>Carrying Value</u>	<u>Fair Value</u>	<u>Rating as of Year End</u>		
			<u>AAA</u>	<u>Aa</u>	<u>Unrated</u>
County Pool Investments	\$ 12,995	\$ 13,015			\$ 12,995

Concentration of Credit Risk

The investment policy of the District contains no limitations on the amount that can be invested in any one issuer beyond the amount stipulated by the California Government Code. However, the District does not hold any investments in any one issuer, at year-end, that represents five percent or more of the total investments held by the District.

Custodial Credit Risk - Deposits

This is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District does not have a policy for custodial credit risk for deposits. However, the California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110 percent of the total amount deposited by the public agencies. California law also allows financial institutions to secure public deposits by pledging first trust deed mortgage notes having a value of 150 percent of the secured public deposits and letters of credit issued by the Federal Home Loan Bank of San Francisco having a value of 105 percent of the secured deposits.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 2 - DEPOSITS AND INVESTMENTS (CONCLUDED)

Custodial Credit Risk - Investments

This is the risk that in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral securities that are in possession of an outside party. The District does not have a policy limiting the amount of securities that can be held by counterparties. As of June 30, 2012, the District does not have any investments that are held by counterparties.

Derivative Investments

The District does not directly invest in any derivative investments. Information relating to the use of derivative investments by the Sonoma County Treasury was not available.

NOTE 3 - EXCESS OF EXPENDITURES OVER APPROPRIATIONS

Excess of expenditures over appropriations in the General Fund were as follows:

<u>General Fund</u>	<u>Excess Expenditures</u>
Capital Outlay	\$ 1,605
Debt Service: Interest and Fiscal Charges	25,604

The District incurred unanticipated expenditures in each of the above expenditure classifications for which the budget was not revised.

NOTE 4 - RECEIVABLES

Receivables at June 30, 2012, consist of the following:

	<u>General Fund</u>	<u>Non-Major Governmental Funds</u>	<u>Total Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Fiduciary Funds</u>
Federal Government	\$ 2,399,972	\$ 182,039	\$ 2,582,011		
State Government	9,783,253	222,691	10,005,944		
Local Governments	2,409,546	128,402	2,537,948		
Miscellaneous	927,691	103,571	1,031,262	\$ 1,020	\$ 233
Totals	<u>\$ 15,520,462</u>	<u>\$ 636,703</u>	<u>\$ 16,157,165</u>	<u>\$ 1,020</u>	<u>\$ 233</u>

NOTE 5 - INTERFUND ACTIVITIES

Interfund transactions are reported as either loans, services provided, reimbursements, or transfers. Loans are reported as interfund receivables and payables, as appropriate, and are subject to elimination upon consolidation. Services provided, deemed to be at market or near market rates, are treated as revenues and expenditures/expenses. Reimbursements occur when one fund incurs a cost, charges the appropriate benefiting fund, and reduces its related cost as a reimbursement. All other interfund transactions are treated as transfers.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 5 - INTERFUND ACTIVITIES (CONCLUDED)

Due From/Due To Other Funds

Individual fund interfund receivable and payable balances at June 30, 2012 are as follows:

<u>Funds</u>	<u>Interfund Receivables</u>	<u>Interfund Payables</u>
General	\$ 5,953,168	\$ 6,709,949
Deferred Maintenance	1,858,068	621,224
Cafeteria	16,555	605,482
Adult Education	1,089,163	1,164,419
Capital Facilities Building	188,402	36,252
County School Facilities	17,779	55,816
Capital Projects - Special Reserve	<u>758,131</u>	<u>779,944</u>
Subtotals	9,881,266	9,973,086
Self-Insurance	<u>91,820</u>	<u> </u>
Totals	<u>\$ 9,973,086</u>	<u>\$ 9,973,086</u>

All interfund receivables and payables are scheduled to be paid within one year.

NOTE 6 - CAPITAL ASSETS AND DEPRECIATION

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

A. Governmental Activities

	<u>Balances July 1, 2011</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balances June 30, 2012</u>
Land	\$ 4,266,886			\$ 4,266,886
Sites and Improvements	12,580,090	\$ 1,851,986		14,432,076
Buildings and Improvements	136,638,241			136,638,241
Furniture and Equipment	6,131,949	269,412		6,401,361
Work-in-Progress	506,298	305,670	\$ 39,736	772,232
Totals at Historical Cost	<u>160,123,464</u>	<u>2,427,068</u>	<u>39,736</u>	<u>162,510,796</u>
Less Accumulated Depreciation for:				
Sites and Improvements	5,061,975	785,119		5,847,094
Buildings and Improvements	46,434,539	4,061,361		50,495,900
Furniture and Equipment	4,841,014	306,815		5,147,829
Total Accumulated Depreciation	<u>56,337,528</u>	<u>5,153,295</u>	<u>0</u>	<u>61,490,823</u>
Governmental Activities Capital Assets, net	<u>\$ 103,785,936</u>	<u>\$ (2,726,227)</u>	<u>\$ 39,736</u>	<u>\$ 101,019,973</u>

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 6 - CAPITAL ASSETS AND DEPRECIATION (CONCLUDED)

A. Governmental Activities (Concluded)

Depreciation expense was charged to governmental activities as follows:

Instruction	\$ 4,002,640
Supervision of Instruction	95,942
Instructional Library and Technology	194,844
School Site Administration	57,466
Home-To-School Transportation	169,291
Food Services	40,723
Other Pupil Services	1,545
Other General Administration	479,205
Plant Services	69,998
Ancillary Services	25,990
Community Services	<u>15,651</u>
Total Depreciation Expense	<u>\$ 5,153,295</u>

B. Business-Type Activities

	<u>Balances</u> <u>July 1, 2011</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balances</u> <u>June 30, 2012</u>
Furniture and Equipment	\$ 56,833			56,833
Totals at Historical Cost	56,833	\$ 0	\$ 0	56,833
Less Accumulated Depreciation for:				
Furniture and Equipment	\$ 26,992	5,687		32,679
Total Accumulated Depreciation	26,992	5,687	0	32,679
Business-Type Activities				
Capital Assets, net	\$ 29,841	\$ (5,687)	\$ 0	\$ 24,154

Depreciation expense was charged to business-type activities as follows:

Enterprise	<u>\$ 5,687</u>
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NOTE 7 - GENERAL OBLIGATION BONDS

On November 1, 2011, the District issued \$8,470,000 of general obligation refunding bonds for purposes of refunding a portion of the District's outstanding bonds with a principal balance of \$8,695,000, and to pay costs of issuance related to the new bonds. The refunding bonds were issued to lower the debt service requirements of the District and reduce the tax burden on the property owners within the District.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 7 - GENERAL OBLIGATION BONDS (CONTINUED)

The outstanding general obligation debt of the District as of June 30, 2012 is as follows:

A. Current Interest Bonds

Description and Date	Interest Rate %	Maturity Year	Amount of Original Issue	Outstanding July 1, 2011	Issued Current Year	Redeemed Current Year	Outstanding June 30, 2012
Elementary							
1991 Series							
2002 I	1.70-5.00	2027	\$ 3,500,000	\$ 2,825,000		\$ 2,825,000	
2004 J	4.00-8.00	2028	2,700,000	2,255,000		85,000	\$ 2,170,000
2003 Series							
(Refunding)	2.75-4.30	2021	5,895,000	3,930,000		3,930,000	
2003 Series B							
(Refunding)	3.00-4.00	2017	4,560,000	2,700,000		2,700,000	
2008 Series							
(Refunding)	2.00-3.80	2024	7,965,000	6,620,000		630,000	5,990,000
2011 Series							
(Refunding)	3.00-4.00	2027	<u>8,470,000</u>	<u>0</u>	<u>\$ 8,470,000</u>	<u>70,000</u>	<u>8,400,000</u>
Total Elementary			<u>33,090,000</u>	<u>18,330,000</u>	<u>8,470,000</u>	<u>10,240,000</u>	<u>16,560,000</u>
High School							
1992 Series							
2010 G	2.00-4.25	2025	2,418,791	2,418,791		3,791	2,415,000
2005 Series							
(Refunding)	3.125-7.00	2024	14,825,000	13,845,000		525,000	13,320,000
2010 Series							
(Refunding)	2.00-4.00	2020	<u>9,095,000</u>	<u>9,095,000</u>		<u>410,000</u>	<u>8,685,000</u>
Total High School			<u>26,338,791</u>	<u>25,358,791</u>	<u>0</u>	<u>938,791</u>	<u>24,420,000</u>
Total Current Interest Bonds			<u>\$59,428,791</u>	<u>\$43,688,791</u>	<u>\$ 8,470,000</u>	<u>\$11,178,791</u>	<u>\$ 40,980,000</u>

The annual requirements to amortize the current interest bonds payable, outstanding as of June 30, 2012, are as follows:

Year Ended June 30	Principal	Interest	Totals
2013	\$ 2,495,000	\$ 1,488,897	\$ 3,983,897
2014	2,555,000	1,411,175	3,966,175
2015	2,490,000	1,329,425	3,819,425
2016	2,560,000	1,237,731	3,797,731
2017	2,670,000	1,136,694	3,806,694
2018-2022	21,065,000	3,895,858	24,960,858
2023-2027	6,625,000	595,616	7,220,616
2028-2032	<u>520,000</u>	<u>19,470</u>	<u>539,470</u>
Totals	<u>\$ 40,980,000</u>	<u>\$ 11,114,866</u>	<u>\$ 52,094,866</u>

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 7 - GENERAL OBLIGATION BONDS (CONCLUDED)

B. Capital Appreciation Bonds

Description and Date	Interest Rate %	Maturity Year	Amount of Original Issue	Outstanding July 1, 2011	Accreted Current Year	Redeemed Current Year	Outstanding June 30, 2012
High School							
1995 Series							
(Refunding)	4.65-5.80	2018	<u>\$ 8,972,019</u>	<u>\$14,846,668</u>	<u>\$ 755,060</u>	<u>\$ 1,375,000</u>	<u>\$ 14,226,728</u>
Total Capital Appreciation Bonds			<u>\$ 8,972,019</u>	<u>\$14,846,668</u>	<u>\$ 755,060</u>	<u>\$ 1,375,000</u>	<u>\$ 14,226,728</u>

The outstanding obligation for the 1995 Series Refunding capital appreciation bonds at June 30, 2012, is as follows:

Year Ended June 30	Rate %	Amount of Original Issue (Principal)	Accreted Interest	Totals
2013		\$ 604,211	\$ 943,541	\$ 1,547,752
2014		638,838	1,010,845	1,649,683
2015		750,699	1,141,508	1,892,207
2016		783,511	1,191,426	1,974,937
2017		800,922	1,234,208	2,035,130
2018-2019		<u>2,017,700</u>	<u>3,109,319</u>	<u>5,127,019</u>
Totals		<u>\$ 5,595,881</u>	<u>\$ 8,630,847</u>	<u>\$ 14,226,728</u>

The annual requirements to amortize the 1995 Series Refunding capital appreciation bonds at June 30, 2012, are as follows:

Year Ended June 30	Principal	Interest	Totals
2013	\$ 604,211	\$ 950,789	\$ 1,555,000
2014	638,838	1,116,162	1,755,000
2015	750,699	1,374,301	2,125,000
2016	783,511	1,561,489	2,345,000
2017	800,922	1,759,078	2,560,000
2018-2019	<u>2,017,700</u>	<u>5,002,300</u>	<u>7,020,000</u>
Totals	<u>\$ 5,595,881</u>	<u>\$ 11,764,119</u>	<u>\$ 17,360,000</u>

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 8 - DEFEASED DEBT

Certain general obligation bonds of the District have been defeased by placing the proceeds of refunding bonds in irrevocable escrow accounts held and managed by bank trustees, the principal and interest on which would provide amounts sufficient to pay the principal and interest on the defeased bonds in accordance with the schedule of remaining payments due. Accordingly, the escrow account and the defeased bonds are not included in the District's financial statements. The defeased bonds outstanding at June 30, 2012 considered extinguished are as follows:

<u>Bond Series</u>	<u>Maturities Refunded</u>	<u>Principal Refunded</u>
1991 Election, Series I	2012-2027	\$ 2,710,000
2003 Refunding	2012-2021	3,610,000
2003 Refunding, Series B	2012-2017	2,375,000

NOTE 9 - CERTIFICATES OF PARTICIPATION

In February 2010, the District issued certificates of participation in the amount of \$7,760,000 with a variable interest rates ranging from 0.18 percent to 0.45 percent to refund the 2005 certificates of participations. As of June 30, 2012, the principal balance outstanding was \$7,205,000. The certificates mature through 2031 as follows:

<u>Year Ended June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Totals</u>
2013	\$ 290,000	\$ 223,857	\$ 513,857
2014	300,000	214,145	514,145
2015	305,000	204,272	509,272
2016	315,000	194,074	509,074
2017	325,000	183,553	508,553
2018-2022	1,775,000	748,618	2,523,618
2023-2027	2,040,000	436,060	2,476,060
2028-2032	1,855,000	92,262	1,947,262
Totals	<u>\$ 7,205,000</u>	<u>\$ 2,296,841</u>	<u>\$ 9,501,841</u>

NOTE 10 - CAPITAL LEASES

The District has entered into a variety of lease-purchase agreements to finance the acquisition of vehicles, equipment, and a solar photovoltaic system valued at \$3,650,170. All of these agreements provide for title to pass upon the expiration of the lease periods.

Future minimum lease payments under these agreements are as follows:

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 10 - CAPITAL LEASES (CONCLUDED)

Year Ended <u>June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Totals</u>
2013	\$ 246,546	\$ 190,101	\$ 436,647
2014	253,435	177,488	430,923
2015	231,358	162,778	394,136
2016	205,500	148,843	354,343
2017	213,797	136,078	349,875
2018-2022	1,205,666	470,111	1,675,777
2023-2027	846,623	92,492	939,115
Totals	<u>\$ 3,202,925</u>	<u>\$ 1,377,891</u>	<u>\$ 4,580,816</u>

The District will receive no sublease rental revenues nor pay any contingent rentals for the leased assets.

NOTE 11 - EARLY RETIREMENT INCENTIVES

The District contributes to the Public Agency Retirement System (PARS), a supplemental retirement plan to STRS administered by PARS. The plan provides a supplemental benefit to STRS and payments are fixed at retirement and do not increase thereafter (No COLA). Payouts are made based on the option determined by the participants and may or may not include payments to their beneficiary depending on the option chosen. The District entered into a multi-year annuity to make contributions to the PARS Supplementary Retirement Plan.

Future payments required to provide this plan are as follows:

Year Ended <u>June 30</u>	<u>PARS Payment</u>
2013	\$ 204,627
2014	204,627

NOTE 12 - OTHER POST-EMPLOYMENT BENEFITS (OPEB)

Plan Descriptions: The Post-Employment Benefit (the "Plan") is a single-employer defined benefit healthcare plan administered by Petaluma City Schools. The Plan provides medical insurance benefits to eligible retirees and their spouses. Eligible employees are those who retired from the District before 2004 upon attaining age 55 with at least 10 years of service. Benefits are paid by the District until the retiree reaches the age of 65 and are capped at negotiated amounts. As of June 30, 2012, membership of the Plan consists of 27 retirees and beneficiaries currently receiving benefits, no terminated plan members entitled to but not yet receiving benefits, and no active plan members.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 12 - OTHER POST-EMPLOYMENT BENEFITS (OPEB) (CONCLUDED)

Contribution Information: The contribution requirements of plan members and the District are established and may be amended by the District and the Teachers Association (CEA), the local California Service Employees Association (CSEA), and unrepresented groups. The required contribution is based on projected pay-as-you-go financing requirements, with an additional amount to refund benefits as determined annually through the agreements between the District, CEA, CSEA and the unrepresented groups. For fiscal year 2011-12, the District contributed \$70,019 to the plan, all of which was used for current premiums (approximately 100 percent of total premiums). The remainder of the premiums were funded from beginning net assets and interest earnings.

Future estimated payments required under the plan are as follows:

Year Ended <u>June 30</u>	Other Post-Employment <u>Benefits</u>
2013	\$ 73,140
2014	43,864
2015	38,078
2016	37,997
2017	37,745
Total	<u>\$ 230,824</u>

Funding Status and Funding Progress: The District uses the Alternative Measurement Method for valuations of the ongoing plan and the measurement methods involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about investment returns, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the Plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multiyear trend information about whether the value of plan assets is increasing or decreasing over time relative to the accrued liabilities for benefits.

Valuation Methods and Assumptions: The projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in accrued liabilities and the value of assets, consistent with the long-term perspective of the calculations.

In the June 30, 2012, valuation measurement, the alternative measure method was used. Healthcare cost trend rates ranged from current actual amounts up to the agreed upon caps. Mortality estimates were not included as the District pays the healthcare benefits only to age 65. The UAAL was fully amortized and no phase in is being applied. There were no assets set aside to fund future amounts.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 13 - LONG-TERM LIABILITIES

A schedule of changes in long-term liabilities for the year ended June 30, 2012, is shown below:

	Balances 7/1/2011 *	Additions	Deductions	Balances June 30, 2012	Due within One Year
Compensated Absences	\$ 453,628	\$ 508,140	\$ 453,628	\$ 508,140	\$ 508,140
General Obligation Bonds:					
Current Interest *	43,688,791	8,470,000	11,178,791	40,980,000	2,495,000
Capital Appreciation *	14,846,668	755,060	1,375,000	14,226,728	1,547,752
Bond Premium *	336,283	452,429	43,910	744,802	60,640
Certificates of Participation	7,485,000		280,000	7,205,000	290,000
Capital Leases	3,482,034	23,873	302,982	3,202,925	246,546
Early Retirement Incentives	0	409,254		409,254	204,627
Other Post-Employment Benefits	300,843		70,019	230,824	73,140
Totals *	<u>\$ 70,593,247</u>	<u>\$ 10,618,756</u>	<u>\$ 13,704,330</u>	<u>\$ 67,507,673</u>	<u>\$ 5,425,845</u>

* Prior year balances have been adjusted to reflect the restatement discussed at Note 22 in these financial statements.

NOTE 14 - FUND BALANCES

The fund balances as of June 30, 2012 are as follows:

	General Fund	Bond Interest & Redemption Fund	Non-Major Governmental Funds	Totals
Nonspendable	\$ 57,771		\$ 21,944	\$ 79,715
Restricted	1,673,360	\$ 5,306,302	1,775,756	8,755,418
Assigned	930,298		1,640,224	2,570,522
Unassigned:				
Economic Uncertainties	1,994,013			1,994,013
Other	7,780,017			7,780,017
Total Fund Balances	<u>\$ 10,441,446</u>	<u>\$ 5,306,302</u>	<u>\$ 3,437,924</u>	<u>\$ 21,179,685</u>

NOTE 15 - ON-BEHALF PAYMENTS MADE BY THE STATE OF CALIFORNIA

The District was the recipient of on-behalf payments made by the State of California to the California State Teachers' Retirement System (CalSTRS) for K-12 education. These payments consist of state general fund contributions of \$1,453,930 to CalSTRS (4.855% of creditable compensation subject to CalSTRS).

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 16 - EMPLOYEE RETIREMENT SYSTEMS

Qualified employees are covered under multiple-employer defined benefit pension plans maintained by agencies of the State of California. Certificated employees are members of the California State Teachers' Retirement System (CalSTRS) and classified employees are members of the California Public Employees' Retirement System (CalPERS).

A. California State Teachers' Retirement System (CalSTRS)

Plan Description

The District contributes to the California State Teachers' Retirement System (CalSTRS), a cost-sharing multiple-employer public employee retirement system defined benefit pension plan administered by CalSTRS. The plan provides retirement, disability, and survivor benefits to beneficiaries. Benefit provisions are established by state statutes, as legislatively amended, within the State Teachers' Retirement Law. CalSTRS issues a separate comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the CalSTRS annual financial report may be obtained from CalSTRS, 100 Waterfront Place, West Sacramento, California 95605.

Funding Policy

Active plan members are required to contribute 8.0% of their salary and the District is required to contribute an actuarially determined rate. The actuarial methods and assumptions used for determining the rate are those adopted by the CalSTRS Teachers' Retirement Board. The required employer contribution rate for fiscal year 2011-12 was 8.25% of annual payroll. The contribution requirements of the plan members are established by state statute. The District's contributions to STRS for the fiscal year ending June 30, 2012, 2011, and 2010, were \$2,407,706, \$2,365,341, and \$2,480,023, respectively, and equal 100% of the required contributions for each year.

B. California Public Employees' Retirement System (CalPERS)

Plan Description

The District contributes to the School Employer Pool under California Public Employees' Retirement System (CalPERS), a cost-sharing multiple-employer public employee retirement system defined benefit pension plan administered by CalPERS. The plan provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by state statutes, as legislatively amended, within the Public Employees' Retirement Law. CalPERS issue a separate comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the CalPERS annual financial report may be obtained from the CalPERS Executive Office, 400 Q Street, Sacramento, California 95811.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 16 - EMPLOYEE RETIREMENT SYSTEMS (CONTINUED) (CONCLUDED)

B. California Public Employees' Retirement System (CalPERS) (Concluded)

Funding Policy

Active plan members are required to contribute 7.0% of their salary, and the District is required to contribute an actuarially determined rate. The actuarial methods and assumptions used for determining the rate are those adopted by the CalPERS Board of Administration. The required employer contribution rate for fiscal year 2011-12 was 10.923% of annual payroll. The contribution requirements of the plan members are established by State statute. The District's contributions to CalPERS for the fiscal year ending June 30, 2012, 2011, and 2010, were \$1,087,622, \$1,130,429, and \$1,057,428, respectively, and equal 100% of the required contributions for each year.

C. Social Security / Tax Deferred Annuity

As established by Federal law, all public sector employees who are not members of their employer's existing retirement system (CalSTRS or CalPERS) must be covered by social security or an alternative plan. The District has elected to use TDA as its alternative plan. Contributions made by the District and participating employees vest immediately. The District contributes 6.2% of an employee's gross earnings. In addition, the employees were required to contribute 4.2% of their gross earnings from July 2011 through June 2012.

The District also has a 403(b) Tax Deferred Annuity Plan (TDA), which is a defined contribution pension plan. A defined contribution pension plan provides pension benefits in return for services rendered, provides an individual account for each participant, and specifies how contributions to the individual's account are to be determined instead of specifying the amount of benefits the individual is to receive. Under a defined contribution pension plan, the benefits a participant will receive depend solely on the amount contributed to the participant's account, the returns earned on investments of those contributions, and forfeitures of other participants' benefits that may be allocated to such participant's account. The 403(b) plan is available for salary deferrals; however, no District contributions are made.

NOTE 17 - RISK MANAGEMENT

The District is exposed to various risks of loss related to theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During fiscal year 2011-12, the District participated in Redwood Empire Schools Insurance Group (RESIG) for purposes of pooling risk. There were no significant reductions in coverage during the year.

NOTE 18 - JOINT VENTURES

The District participates in three joint ventures under joint powers agreements (JPAs); the Redwood Empire Schools Insurance Group (RESIG) for workers' compensation, property and liability, and dental coverage, the Schools Excess Liability Fund public entity risk pools for excess liability, and the School Project for Utility Rate Reduction joint powers authority (JPA) for direct purchase of gas, electricity, and other utility services. The relationships between the District and the JPAs are such that the JPAs are not component units of the District for financial reporting purposes.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 18 - JOINT VENTURES (CONCLUDED)

The JPAs arrange for and/or provide coverage for its members. Each JPA is governed by a Board, which controls the operations of the JPA, including selection of management and approval of operating budgets independent of any influence by the member districts beyond their representation on the Board. Each member district pays a premium commensurate with the level of coverage requested and shares surpluses and deficits proportionately to their participation in the JPA.

The JPAs are audited on an annual basis. Financial information can be obtained by contacting each JPA's management.

NOTE 19 - CHARTER SCHOOL

The District has approved Charters for the Live Oak Charter School, 6th Grade Charter Academy, and the Mary Collins School at Cherry Valley pursuant to Education Code Section 47605. The 6th Grade Charter Academy and Mary Collins School at Cherry Valley charter schools are operated by the District, and its financial activities are presented in the General Fund. The Live Oak Charter School is responsible for managing, budgeting, and accounting for its activities in accordance with U.S. generally accepted accounting principles and is not considered a component unit of the District. The District receives revenue on behalf of the Live Oak Charter School which it passes on to the Charter School.

NOTE 20 - RECLASSIFICATION OF FUND BALANCES

The beginning fund balance of the General Fund has been split out into General Fund, Deferred Maintenance Fund, and Adult Education Fund for financial reporting purposes in accordance with GASB 54.

	General Fund	Deferred Maintenance Fund	Adult Education Fund
Fund Balances - July 1, 2011 (as originally stated)	\$ 14,577,360	\$ 0	\$ 0
Reclassification of Fund Balances	<u>(1,340,696)</u>	<u>1,060,027</u>	<u>280,669</u>
Fund Balances - July 1, 2011 (as reclassified)	<u>\$ 13,236,664</u> *	<u>\$ 1,060,027</u>	<u>\$ 280,669</u> *

* The reclassified fund balances of these funds have also been restated as discussed in Note 21.

NOTE 21 - RESTATEMENT OF FUND BALANCES

The beginning fund balance of the General Fund was overstated by \$1,169,120, due to the improper recognition of Education Jobs Fund revenues in fiscal year 2010-11, before qualified expenditures had been incurred.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 21 - RESTATEMENT OF FUND BALANCES (CONCLUDED)

The beginning fund balance of the General Fund was understated by \$649,316, due to the District's failure to accrue fiscal year 2010-11 revenues for programs such as supplemental instruction, gifted and talented education, community day school and adult education that were deferred as part of the principal apportionment, yet considered measureable and available for purposes of establishing receivables.

The beginning fund balance of the Adult Education Fund was understated by \$130,024, due to the District's failure to accrue fiscal year 2010-11 revenues for apprenticeship hours provided that were deferred as part of the principal apportionment, yet considered measureable and available for purposes of establishing receivables.

The effect of the restatements on the governmental fund financial statements is as follows:

	General Fund	Adult Education Fund
Fund Balances - July 1, 2011 (as reclassified - Note 20)	\$ 13,236,664	\$ 280,669
Overstatement of Education Jobs Fund Revenues	(1,169,120)	
Understatement of Principal Apportionment Program Revenues	649,316	130,024
Net Restatements	(519,804)	130,024
Fund Balances - July 1, 2011 (as restated)	\$ 12,716,860	\$ 410,693

NOTE 22 - RESTATEMENT OF NET ASSETS

The beginning net assets balance on the government-wide Statement of Activities has been restated to correct the following:

As discussed in Note 21, the beginning fund balance of the General Fund was overstated due to the improper recognition of Education Jobs Fund revenues in fiscal year 2010-11, before qualified expenditures had been incurred. As a result, the beginning net asset balance was overstated by \$1,169,120.

As discussed in Note 21, the beginning fund balance of the General Fund was understated due to the District's prior year failure to accrue fiscal year 2010-11 revenues for programs such as supplemental instruction, gifted and talented education, community day school, and adult education that were deferred as part of the principal apportionment, yet considered measureable and available for purposes of establishing receivables. As a result, the beginning net asset balance was understated by \$649,316.

As discussed in Note 21, the beginning fund balance of the Adult Education Fund was understated due to the District's failure to accrue fiscal year 2010-11 revenues for apprenticeship hours that were deferred as part of the principal apportionment, yet considered measureable and available for purposes of establishing receivables. As a result, the beginning net asset balance was understated by \$130,024.

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 22 - RESTATEMENT OF NET ASSETS (CONCLUDED)

The prior year liability balance reported for outstanding general obligation bonds was overstated due to the inclusion of liabilities related to two separate bond issues that were defeased in prior fiscal years through the bond refunding process, but never removed as liabilities of the District. As a result, the beginning net asset balance was understated by \$4,826,042.

The prior year liability balance reported for unamortized bond premiums was understated due to accounting errors related to prior year bond refunding transactions. As a result, the beginning net asset balance was overstated by \$92,295.

The prior year asset balance reported for unamortized bond issuance costs was overstated due to accounting errors related to prior year bond refunding transactions. As a result, the beginning net asset balance was overstated by \$691,601.

The prior year asset balance reported for unamortized bond refunding costs was understated due to accounting errors related to prior year bond refunding transactions. As a result, the beginning net asset balance was understated by \$1,187,510.

The effects of these restatements on the current year financial statements are as follows:

	<u>Statement of Activities</u>
	<u>Governmental Activities</u>
Net Assets - July 1, 2011 (as originally stated)	\$ <u>51,235,243</u>
Overstatements:	
Education Jobs Fund Revenue	(1,169,120)
General Obligation Bonds Payable	4,826,042
Unamortized Bond Issuance Costs	(691,601)
Understatements:	
General Fund Principal Apportionment Program Revenues	649,316
Adult Education Fund Principal Apportionment Program Revenues	130,024
Unamortized Bond Refunding Costs	1,187,510
Unamortized Bond Premium	<u>(92,295)</u>
Net Restatement	<u>4,839,876</u>
Net Assets - July 1, 2011 (as restated)	<u>\$ 56,075,119</u>

PETALUMA CITY SCHOOLS
NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 23 - COMMITMENTS AND CONTINGENCIES

A. State and Federal Allowances, Awards and Grants

The District has received state and federal funds for specific purposes that are subject to review and audit by the grantor agencies. Although such audits could generate expenditure disallowances under terms of the grants, it is believed that any required reimbursements will not be material.

B. Litigation

The District is subject to various other legal proceedings and claims. In the opinion of management, the ultimate liability with respect to these other actions will not materially affect the financial position or results of operations of the District.

NOTE 24 - SUBSEQUENT EVENT

General Obligation Refunding Bonds

On August 9, 2012, the District issued \$12,845,000 of general obligation refunding bonds for purposes of refunding \$12,775,000 of the District's outstanding 2005 General Obligation Refunding Bonds, maturing on and after August 1, 2013, and to pay costs of issuance of the Bonds. The refunding bonds were issued to take advantage of the current lower interest rates, which will ultimately result in a decreased tax burden for the individuals who own property within the District.

SUPPLEMENTARY INFORMATION SECTION

PETALUMA CITY SCHOOLS
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
BUDGET AND ACTUAL - GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	<u>Original Budget</u>	<u>Final Budget</u>	<u>Actual</u>	<u>Variance with Final Budget Favorable (Unfavorable)</u>
<u>Revenues</u>				
Revenue Limit Sources:				
State Apportionment	\$ 18,583,511	\$ 19,600,696	\$ 16,055,211	\$ (3,545,485)
Local Sources	23,911,384	22,888,475	26,072,024	3,183,549
Total Revenue Limit Sources	42,494,895	42,489,171	42,127,235	(361,936)
Federal Revenue	4,900,539	6,094,044	5,609,532	(484,512)
Other State Revenue	8,610,585	8,923,909	10,276,182	1,352,273
Other Local Revenue	7,887,142	8,624,772	8,172,764	(452,008)
Total Revenues	63,893,161	66,131,896	66,185,713	53,817
<u>Expenditures</u>				
Certificated Salaries	29,709,611	29,512,108	29,498,927	13,181
Classified Salaries	9,794,248	10,186,647	10,147,975	38,672
Employee Benefits	14,115,461	13,954,300	13,889,910	64,390
Books and Supplies	2,084,919	3,589,285	2,746,626	842,659
Services and Other				
Operating Expenditures	10,237,597	10,945,871	9,516,127	1,429,744
Capital Outlay	10,000	263,205	264,810	(1,605)
Debt Service:				
Principal Retirement	321,475	322,575	298,548	24,027
Interest and Fiscal Charges	175,783	177,433	203,037	(25,604)
Other Expenditures	681,715	330,574	(74,973)	405,547
Total Expenditures	67,130,809	69,281,998	66,490,987	2,791,011
Excess of Revenues (Under) Expenditures	(3,237,648)	(3,150,102)	(305,274)	2,844,828
<u>Other Financing Sources</u>				
Other Sources			23,873	23,873
Net Change in Fund Balances	(3,237,648)	(3,150,102)	(281,401)	\$ 2,868,701
Fund Balances - July 1, 2011 (As Reclassified / Restated - Notes 20 & 21)	12,716,860	12,716,860	12,716,860	
Fund Balances - June 30, 2012	\$ 9,479,212	\$ 9,566,758	\$ 12,435,459	

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS

**PETALUMA CITY SCHOOLS
COMBINING BALANCE SHEET
NON-MAJOR GOVERNMENTAL FUNDS
JUNE 30, 2012**

	<u>Deferred Maintenance</u>	<u>Cafeteria</u>	<u>Adult Education</u>
<u>Assets</u>			
Deposits and Investments	\$ 20,956	\$ 608,386	\$ 158,629
Receivables		126,807	415,875
Due from Other Funds	1,858,068	16,555	1,089,163
Stores Inventory		21,494	
Total Assets	<u>\$ 1,879,024</u>	<u>\$ 773,242</u>	<u>\$ 1,663,667</u>
<u>Liabilities and Fund Balances</u>			
Liabilities:			
Accounts Payable	\$ 315,013	\$ 1,331	\$ 169,346
Due to Other Funds	621,224	605,482	1,164,419
Deferred Revenue		15,902	4,828
Total Liabilities	<u>936,237</u>	<u>622,715</u>	<u>1,338,593</u>
Fund Balances:			
Nonspendable		21,644	300
Restricted	1,769	128,883	
Assigned	941,018		324,774
Total Fund Balances	<u>942,787</u>	<u>150,527</u>	<u>325,074</u>
Total Liabilities and Fund Balances	<u>\$ 1,879,024</u>	<u>\$ 773,242</u>	<u>\$ 1,663,667</u>

Capital Facilities	Building	County School Facilities	Capital Projects - Special Reserve	Total Non-Major Governmental Funds
\$ 863,944	\$ 178,105	\$ 62,471	\$ 732,182	\$ 2,624,673
81,084			12,937	636,703
	188,402	17,779	758,131	3,928,098
				21,494
<u>\$ 945,028</u>	<u>\$ 366,507</u>	<u>\$ 80,250</u>	<u>\$ 1,503,250</u>	<u>\$ 7,210,968</u>
	\$ 2,924			\$ 488,614
\$ 36,252	55,816		\$ 779,944	3,263,137
			563	21,293
<u>36,252</u>	<u>58,740</u>		<u>780,507</u>	<u>3,773,044</u>
				21,944
908,776	307,767	\$ 80,250	348,311	1,775,756
			374,432	1,640,224
<u>908,776</u>	<u>307,767</u>	<u>80,250</u>	<u>722,743</u>	<u>3,437,924</u>
<u>\$ 945,028</u>	<u>\$ 366,507</u>	<u>\$ 80,250</u>	<u>\$ 1,503,250</u>	<u>\$ 7,210,968</u>

PETALUMA CITY SCHOOLS
COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND
CHANGES IN FUND BALANCES
NON-MAJOR GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	<u>Deferred Maintenance</u>	<u>Cafeteria</u>	<u>Adult Education</u>
<u>Revenues</u>			
Federal Revenue		\$ 1,104,990	\$ 68,174
State Revenue	\$ 278,086	98,914	873,575
Local Revenue	586,688	786,122	269,467
Total Revenues	<u>864,774</u>	<u>1,990,026</u>	<u>1,211,216</u>
<u>Expenditures</u>			
Instruction			884,486
School Site Administration			271,183
Food Services		1,952,744	
Other Pupil Services			65,299
Other General Administration		71,470	59,839
Plant Services	660,814	5,410	16,028
Facilities Acquisition and Construction	321,200		
Debt Service:			
Principal Retirement		4,434	
Interest and Issuance Costs		835	
Total Expenditures	<u>982,014</u>	<u>2,034,893</u>	<u>1,296,835</u>
Net Change in Fund Balances	(117,240)	(44,867)	(85,619)
Fund Balances - July 1, 2011 (As Reclassified / Restated - Notes 20 & 21)	<u>1,060,027</u>	<u>195,394</u>	<u>410,693</u>
Fund Balances - June 30, 2012	<u>\$ 942,787</u>	<u>\$ 150,527</u>	<u>\$ 325,074</u>

THE ACCOMPANYING NOTES ARE AN INTEGRAL PART OF THESE STATEMENTS

<u>Capital Facilities</u>	<u>Building</u>	<u>County School Facilities</u>	<u>Capital Projects - Special Reserve</u>	<u>Total Non-Major Governmental Funds</u>
				\$ 1,173,164
\$ 470,428	\$ 31,341	\$ 485	\$ 206,174	1,250,575
<u>470,428</u>	<u>31,341</u>	<u>485</u>	<u>206,174</u>	<u>2,350,705</u>
				884,486
				271,183
				1,952,744
				65,299
				131,309
70,602	99	1,626	43,991	798,570
12,608	51,417	76,967	82,620	544,812
			280,000	284,434
			134,309	135,144
<u>83,210</u>	<u>51,516</u>	<u>78,593</u>	<u>540,920</u>	<u>5,067,981</u>
387,218	(20,175)	(78,108)	(334,746)	(293,537)
<u>521,558</u>	<u>327,942</u>	<u>158,358</u>	<u>1,057,489</u>	<u>3,731,461</u>
<u>\$ 908,776</u>	<u>\$ 307,767</u>	<u>\$ 80,250</u>	<u>\$ 722,743</u>	<u>\$ 3,437,924</u>

PETALUMA CITY SCHOOLS
SCHEDULE OF FUNDING PROGRESS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

<u>Actuarial Valuation Date</u>	<u>Value of Assets</u>	<u>Accrued Liability (AAL)</u>	<u>Unfunded AAL (UAAL)</u>	<u>Funded Ratio</u>	<u>Covered Payroll</u>	<u>Percentage of Covered Payroll</u>
06/30/12	\$ 0	\$ 230,824	\$ 230,824	0%	\$ 0	0%
06/30/11	0	300,843	300,843	0%	0	0%
06/30/10	0	454,023	454,023	0%	0	0%

SEE NOTES TO SUPPLEMENTARY INFORMATION

PETALUMA CITY SCHOOLS
ORGANIZATION/BOARD OF EDUCATION/ADMINISTRATION
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

ORGANIZATION

The Petaluma City Schools was established in 1857 under the laws of the State of California. The District operates six elementary schools, one sixth grade charter school, one K-8 charter school, two middle schools, a community day school, two high schools, three continuation schools, one independent study site serving grades K-12, and one adult school. There were no boundary changes during the year.

BOARD OF EDUCATION

<u>Name</u>	<u>Office</u>	<u>Term Expires</u>
Mary Schafer	President	November 2012
Troy Sanderson	Clerk	November 2012
Michael Baddeley	Member	November 2014
Sheri Chlebowski	Member	November 2014
Carolyn Tennyson	Member	November 2014

ADMINISTRATION

Steve Bolman
Superintendent

Midge Hoffman
Chief Business Official

PETALUMA CITY SCHOOLS
SCHEDULE OF AVERAGE DAILY ATTENDANCE
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	P-2 Report		Annual Report	
	District Reported	Audited	District Reported	Audited
<u>Elementary</u>				
Kindergarten	288.88	288.10 *	289.15	289.15
First through Third	922.50	922.47 **	923.09	923.09
Fourth through Sixth	845.68	845.56 **	844.26	844.26
Seventh and Eighth	1,505.36	1,505.35 **	1,502.75	1,502.75
Home and Hospital	1.77	1.77	1.96	1.96
Special Education - SDC	42.14	42.14	43.22	43.22
Special Education - Nonpublic	8.18	8.18	8.59	8.59
Community Day School	9.67	9.67	10.46	10.46
Extended Year	0.76	0.76	1.75	1.75
Subtotals	3,624.94	3,624.00	3,625.23	3,625.23
<u>Secondary</u>				
Nine through Twelve	2,928.92	2,916.73 **	2,897.75	2,897.75
Continuation Education	136.65	136.65	136.65	136.65
Home & Hospital	9.72	9.72	11.73	11.73
Special Education - SDC	39.71	51.94 **	52.02	52.02
Special Education - Nonpublic	13.39	13.39	13.36	13.36
Community Day School	10.32	10.32	9.33	9.33
Extended Year	2.02	2.02	2.32	2.32
Subtotals	3,140.73	3,140.77	3,123.16	3,123.16
Totals	6,765.67	6,764.77	6,748.39	6,748.39

* Reported amount reflects the exclusion of ADA disallowed at 12 - 19 / 10000 in the Findings and Questioned Section of this report.

** Reported amounts reflect District initiated revisions that were not made as a result of the annual audit.

PETALUMA CITY SCHOOLS

SCHEDULE OF AVERAGE DAILY ATTENDANCE - CHARTER SCHOOLS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	<u>P-2 Report</u>		<u>Annual Report</u>	
	<u>Classroom Based</u>	<u>Total</u>	<u>Classroom Based</u>	<u>Total</u>
<u>Sixth Grade Charter Academy</u>				
Fourth through Sixth	56.49	56.56	56.45	56.56
<u>Mary Collins School at Cherry Valley</u>				
Kindergarten	47.83	47.90	47.94	47.99
First through Third	139.73	139.95	138.59	138.91
Fourth through Sixth	125.32	125.47	124.53	124.65
Seven through Eight	74.45	74.57	74.59	74.68
Totals	<u>443.82</u>	<u>444.45</u>	<u>442.10</u>	<u>442.79</u>

PETALUMA CITY SCHOOLS
SCHEDULE OF INSTRUCTIONAL TIME
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

<u>Grade Level</u>	<u>1982-83 Actual Minutes</u>	<u>Adjusted 1982-83 Actual Minutes</u>	<u>1986-87 Minutes Required</u>	<u>Adjusted 1986-87 Minutes Required</u>	<u>2011-12 Actual Minutes</u>	<u>Number of Days Traditional Calendar</u>	<u>Number of Days Multitrack Calendar</u>	<u>Status</u>
Kindergarten	31,500	29,400	36,000	33,600	35,400	177	N/A	In Compliance
Grade 1	42,000	39,200	50,400	47,040	49,750	177	N/A	In Compliance
Grade 2	42,000	39,200	50,400	47,040	49,750	177	N/A	In Compliance
Grade 3	42,000	39,200	50,400	47,040	49,750	177	N/A	In Compliance
Grade 4	49,875	46,550	54,000	50,400	53,270	177	N/A	In Compliance
Grade 5	49,875	46,550	54,000	50,400	53,270	177	N/A	In Compliance
Grade 6	49,875	46,550	54,000	50,400	53,270	177	N/A	In Compliance
Grade 7	49,875	46,550	54,000	50,400	53,215	177	N/A	In Compliance
Grade 8	49,875	46,550	54,000	50,400	53,215	177	N/A	In Compliance
Grade 9	56,525	52,757	64,800	60,480	63,815	177	N/A	In Compliance
Grade 10	56,525	52,757	64,800	60,480	63,815	177	N/A	In Compliance
Grade 11	56,525	52,757	64,800	60,480	63,815	177	N/A	In Compliance
Grade 12	56,525	52,757	64,800	60,480	63,815	177	N/A	In Compliance

SEE NOTES TO SUPPLEMENTARY INFORMATION

PETALUMA CITY SCHOOLS
SCHEDULE OF INSTRUCTIONAL TIME - CHARTER SCHOOLS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	<u>2011-12 Minutes</u>		
<u>6th Grade Charter Academy</u>	<u>Requirement</u>	<u>Actual</u>	<u>Status</u>
Grade 6	50,297	53,265	In Compliance
 <u>Mary Collins School at Cherry Valley</u>			
Kindergarten	33,531	37,065	In Compliance
Grade 1	46,944	49,410	In Compliance
Grade 2	46,944	49,410	In Compliance
Grade 3	46,944	49,410	In Compliance
Grade 4	50,297	53,230	In Compliance
Grade 5	50,297	53,230	In Compliance
Grade 6	50,297	53,230	In Compliance
Grade 7	50,297	53,230	In Compliance
Grade 8	50,297	53,230	In Compliance

PETALUMA CITY SCHOOLS

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

<u>Program Name</u>	<u>Federal Catalog Number</u>	<u>Pass-Through Identification Number</u>	<u>Federal Program Expenditures</u>
U.S. Department of Agriculture:			
Passed through California Department of Education (CDE):			
<i>Child Nutrition Cluster:</i>			
National School Lunch	10.555	13524	\$ 809,972
Basic Breakfast	10.553	13525	3,940
Needy Breakfast	10.553	13526	291,078
FMV Commodities	10.555	n/a	95,946
U.S. Department of Education:			
Passed through CDE:			
<i>Adult Education Cluster:</i>			
Adult Basic Education & ESL	84.002A	14508	34,652
Adult Secondary Education	84.002	13978	1,522
English Literacy & Civics	84.002A	14109	32,000
<i>Title I, Part A Cluster:</i>			
NCLB: Title I Basic Grant Low-Income & Neglected	84.010	14329	605,893
NCLB: Title I School Improvement Grant	84.377	14971	6,154
Education Jobs Fund	84.410	25152	1,406,868
Carl D. Perkins Career and Technical Education	84.243	14899	42,232
NCLB: Title II Improving Teacher Quality	84.367	14341	237,028
NCLB: Title II Administrator Training	84.367	14344	13,578
NCLB: Title III Immigrant Education Program	84.365	14346	3,889
NCLB: Title III Limited English Proficient	84.365	10084	179,452
NCLB: Title V Innovative Education Strategies	84.298A	14354	222
NCLB: Title X McKinney-Vento Homeless Assistance	84.196	14332	7,279
Passed through Sonoma County SELPA:			
<i>Special Education Cluster:</i>			
IDEA Part B Local Assistance	84.027	13379	1,630,371
IDEA Part B Preschool Grants	84.173	13430	151,081
IDEA Part B Preschool Local Entitlement	84.027A	13682	135,227
ARRA IDEA Part B Local Assistance	84.391	15003	195,444
ARRA IDEA Part B Preschool Grants	84.392	15000	19,081
ARRA IDEA Part B Preschool Local Entitlement	84.391	15002	62,785
IDEA Part B Mental Health Allocation	84.027	14468	101,070
IDEA Part B Preschool Staff Development	84.173A	13431	1,644
Received Direct:			
Traditional Teaching American History Project	84.215X	n/a	284,276
Readiness and Emergency Management	84.184E	n/a	284,177
Smaller Learning Communities Grant	84.215L	n/a	228,753
U.S. Department of Health and Human Services:			
Passed through California Department of Health Services:			
Medi-Cal Billing	93.778	10013	2,553
Passed through Sutter County Office of Education:			
Medi-Cal Administrative Activities	93.778	10060	13,026
Total			<u>\$ 6,881,193</u>

SEE NOTES TO SUPPLEMENTARY INFORMATION

PETALUMA CITY SCHOOLS
RECONCILIATION OF ANNUAL FINANCIAL AND BUDGET REPORT
WITH AUDITED FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	Governmental Activities				Business - Type Activities
	General Fund	Deferred Maintenance Fund	Adult Education Fund	Capital Projects- Special Reserve Fund	Enterprise Fund
June 30, 2012 Annual Financial and Budget Report Fund Balances	\$12,976,724	\$ 970,371	\$ 452,312	\$ 701,275	\$ 10,649
Adjustments Increasing (Decreasing) Fund Balances:					
Overstatement of State Aid	(263,179)				
Overstatement of State Revenue	(278,086)		(127,238)		
Understatement of State Revenue		278,086			
Understatement of Services and Other Operating Expenditures		(305,670)			
Understatement of Cash with Fiscal Agent				21,468	
Understatement of Furniture and Equipment					56,833
Understatement of Accumulated Depreciation					(32,679)
Net Adjustments	(541,265)	(27,584)	(127,238)	21,468	24,154
June 30, 2012 Audited Financial Statements Fund Balances	<u>\$12,435,459</u>	<u>\$ 942,787</u>	<u>\$ 325,074</u>	<u>\$ 722,743</u>	<u>\$ 34,803</u>
				Private-Purpose Trust	
				Scholarship Fund	
June 30, 2012 Annual Financial and Budget Report Fund Balances					\$ 106,766
Adjustment (Decreasing) Fund Balance:					
Overstatement of Cash on Hand and in Bank					(4,548)
June 30, 2012 Audited Financial Statements Fund Balance					<u>\$ 102,218</u>

Auditor's Comments

The audited financial statements of all other funds were in agreement with the Annual Financial and Budget Report for the fiscal year ended June 30, 2012.

PETALUMA CITY SCHOOLS

SCHEDULE OF FINANCIAL TRENDS AND ANALYSIS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	GENERAL FUND			
	(Budget)* 2012-13	2011-12	2010-11	2009-10
Revenues and Other Financial Sources	\$ 62,460,002	\$ 66,209,586	\$ 66,813,461 ***	\$ 68,491,526
Expenditures	63,496,087	66,490,987	64,476,607	67,065,771
Other Uses and Transfers Out	0	0	939,911	917,574
Total Outgo	63,496,087	66,490,987	65,416,518	67,983,345
Change in Fund Balance	(1,036,085)	(281,401)	1,396,943 ***	508,181
Ending Fund Balance	\$ 11,399,374	\$ 12,435,459	\$ 12,716,860 ***	\$ 11,319,917
Available Reserves	\$ 9,964,691	\$ 9,774,030	\$ 10,101,321	\$ 9,706,762
Reserve for Economic Uncertainties **	\$ 1,904,883	\$ 1,994,013	\$ 1,962,496	\$ 2,039,500
Available Reserves as a Percentage of Total Outgo	15.7%	14.7%	15.4%	14.3%
Total Long-Term Liabilities	\$ 62,081,828	\$ 67,507,673	\$ 70,593,247 ***	\$ 72,809,210 ***
Average Daily Attendance at P-2 (Inclusive of Charter School ADA)	7,267	7,209	7,217	7,255

* The fiscal year 2012-13 budget information is presented for analytical purposes only and has not been audited.

** The reported balances are a component of available reserves.

*** The reported balances have been adjusted to reflect the restatements discussed at Notes 21 & 22, as applicable.

The fund balance of the General Fund increased \$1,115,542 (9.9%) over the past two years. The fiscal year 2012-13 budget projects a decrease of \$1,036,085 (8.3%). For a district this size, the state recommends available reserves of at least 3% of total General Fund expenditures, transfers out, and other uses (total outgo).

The District produced operating surpluses of \$508,181 and \$1,396,943 during fiscal years 2009-10 and 2010-11, respectively, and incurred an operating deficit of \$281,401 during fiscal year 2011-12.

Total long-term liabilities decreased \$5,301,537 over the past two years due primarily to the reduction of the District's liabilities related to general obligation bonds.

Average daily attendance (ADA) decreased 46 ADA over the past two years. The District anticipates an increase of 58 ADA during fiscal year 2012-13.

**PETALUMA CITY SCHOOLS
SCHEDULE OF CHARTER SCHOOLS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012**

<u>Charter School</u>	<u>District Audit</u>
6 th Grade Charter Academy	Included
Mary Collins School at Cherry Valley	Included
Live Oak Charter	Excluded

PETALUMA CITY SCHOOLS
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
MEASURE C & MEASURE K - PARCEL TAX
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

	<u>Elementary Measure C</u>	<u>High School Measure K</u>	<u>Totals</u>
<u>Revenues</u>			
Parcel Tax Revenue, Net	\$ 745,683	\$ 1,148,731	\$ 1,894,414
<u>Expenditures</u>			
Certificated Salaries	393,283	345,199	738,482
Classified Salaries	116,253	113,318	229,571
Employee Benefits	179,860	165,228	345,088
Books and Supplies	86,104	251,466	337,570
Services and Operating Expenditures	14,317	84,353	98,670
Total Expenditures	789,817	959,564	1,749,381
Net Change in Fund Balances	(44,134)	189,167	145,033
Fund Balances - Beginning	394,255	386,998	781,253
Fund Balances - Ending	<u>\$ 350,121</u>	<u>\$ 576,165</u>	<u>\$ 926,286</u>

SEE NOTES TO SUPPLEMENTARY INFORMATION

PETALUMA CITY SCHOOLS
NOTES TO SUPPLEMENTARY INFORMATION
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - PURPOSE OF STATEMENTS AND SCHEDULES

A. Schedule of Revenues, Expenditures, and Changes in Fund Balances - Budget and Actual

In accordance with Governmental Accounting Standards Board (GASB) Statement No. 34, the District is required to present a Schedule of Revenues, Expenditures, and Changes in the Fund Balances budgetary comparison for the General Fund and each Major Special Revenue Fund that has an adopted budget. This schedule presents the original adopted budget, final adopted budget, and the actual revenues and expenditures of each of these funds by object.

B. Combining Statements

Combining statements are presented for purposes of additional analysis, and are not a required part of the District's basic financial statements. These statements present more detailed information about the financial position and financial activities of the District's individual funds.

C. Schedule of Funding Progress

In accordance with Governmental Accounting Standards Board (GASB) Statement No. 45, the District is required to present a Schedule of Funding Progress which shows the funding progress of the District's OPEB plan for the most recent valuation and the two preceding valuations. The information required to be disclosed includes the valuation date, the actuarial value of assets, the actuarial accrued liability, the total unfunded actuarial liability (or funding excess), the actuarial value of assets as a percentage of the actuarial accrued liability (funded ratio), the annual covered payroll and the ratio of the unfunded actuarial liability (or funding excess) to annual covered payroll.

D. Schedule of Average Daily Attendance

Average daily attendance is a measurement of the number of pupils attending classes of the District. The purpose of attendance accounting from a fiscal standpoint is to provide the basis on which apportionments of state funds are made to school districts. This schedule provides information regarding the attendance of students at various grade levels and in different programs.

E. Schedule of Average Daily Attendance - Charter Schools

The average daily attendance is a measurement of the number of pupils attending classes at District operated Charter Schools. The purpose of attendance accounting from a fiscal standpoint is to provide the basis on which apportionments of state funds are made to the charter school. This schedule provides information regarding the attendance of classroom-based and nonclassroom-based students at various grade levels at the 6th Grade Charter Academy and Mary Collins School at Cherry Valley charter schools.

PETALUMA CITY SCHOOLS
NOTES TO SUPPLEMENTARY INFORMATION
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - PURPOSE OF STATEMENTS AND SCHEDULES (CONTINUED)

F. Schedule of Instructional Time

The District has received incentive funding for increasing instructional time as provided by the Incentives for Longer Instructional Day. This schedule presents information on the amount of instructional time offered by the District and whether the District complied with the provisions of Education Code Sections 46200 through 46206.

G. Schedule of Instructional Time - Charter Schools

Education Code Section 47612.5 requires classroom-based charter schools to offer a minimum number of minutes of instruction. For fiscal years 2011-12 through 2012-13, the minimum number of instructional time is reduced pursuant to the provisions of Education Code Section 46201.2. This schedule presents information on the amount of instructional time offered by the 6th Grade Charter Academy and the Mary Collins School at Cherry Valley and whether the charter schools complied with the provisions of Education Code Section 47612.5(a)(1), as reduced by the provisions of Education Code Section 46201.2.

H. Schedule of Expenditures of Federal Awards

The accompanying schedule of expenditures of federal awards includes the federal grant activities of the District and is presented on the modified 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*.

I. Reconciliation of Annual Financial and Budget Report with Audited Financial Statements

This schedule provides the information necessary to reconcile the fund balances of all funds as reported in the Annual Financial and Budget Report to the audited financial statements.

J. Schedule of Financial Trends and Analysis

This schedule is presented to improve the evaluation and reporting of the going concern status of the District. These financial trend disclosures are used to evaluate the District's ability to continue as a going concern for a reasonable period of time.

K. Schedule of Charter Schools

This schedule lists all charter schools chartered by the District and identifies whether or not the charter schools were included or excluded from the audit of the District.

L. Schedule of Parcel Tax

These statements provide information regarding the receipt and use of funds related to the Measure C and Measure K parcel taxes, and the Maintaining Excellence in Jr. High and High Schools Act of 2007 Tax.

PETALUMA CITY SCHOOLS
NOTES TO SUPPLEMENTARY INFORMATION
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

NOTE 1 - PURPOSE OF STATEMENTS AND SCHEDULES (CONCLUDED)

L. Schedule of Parcel Tax (Concluded)

The Measure C and Measure K parcel tax measures were approved by the voters on November 2, 2004 for the Petaluma Elementary School District and the Petaluma High School District, respectively. On May 8, 2007, revisions to the measures, known as the Maintaining Excellence in Jr. High and High Schools Act of 2007 Tax, were approved by the voters. These revisions retained the same purposes and other terms of the measures but extended the time frame from four years to indefinite.

The Elementary School parcel tax is used for the following: keeping libraries open; continuing to provide reading specialists; continuing smaller class sizes, music and art programs; computer and technology programs; providing necessary educational programs and materials; and attracting and retaining qualified teachers.

The High School parcel tax is used for the following: keeping libraries open; continuing smaller class sizes; computer and technology programs; music and fine art programs; and attracting and retaining qualified teachers.

OTHER INDEPENDENT AUDITOR'S REPORTS SECTION

STEPHEN ROATCH ACCOUNTANCY CORPORATION

Certified Public Accountants

INDEPENDENT AUDITOR'S REPORT ON STATE COMPLIANCE

Board of Education
Petaluma City Schools
Petaluma, California

We have audited Petaluma City Schools' compliance with the types of compliance requirements described in the *Standards and Procedures for Audits of California K-12 Local Educational Agencies 2011-12* to the state laws and regulations listed below for the year ended June 30, 2012. Compliance with the requirements of state laws and regulations is the responsibility of the District's management. Our responsibility is to express an opinion on Petaluma City Schools 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 the *Standards and Procedures for Audits of California K-12 Local Educational Agencies 2011-12* prescribed in the California Code of Regulations, Title 5, section 19810 and following. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the state laws and regulations listed below occurred. An audit includes examining, on a test basis, evidence about Petaluma City Schools' 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 Petaluma City Schools' compliance with those requirements.

<u>Description</u>	Procedures in Education Audit Appeals Panel's <u>Audit Guide</u>	<u>Procedures Performed</u>
Attendance Accounting:		
Attendance Reporting	6	Yes
Teacher Certification and Misassignments	3	Yes
Kindergarten Continuance	3	Yes
Independent Study	23	Yes
Continuation Education	10	Yes
Instructional Time:		
School Districts	6	Yes
County Offices of Education	3	Not Applicable
Instructional Materials:		
General Requirements	8	Yes
Ratios of Administrative Employees to Teachers	1	Yes
Classroom Teacher Salaries	1	Yes
Early Retirement Incentive	4	Not Applicable
Gann Limit Calculation	1	Yes
School Accountability Report Card	3	Yes
Public Hearing Requirement - Receipt of Funds	1	Yes

<u>Description</u>	<u>Procedures In Education Audit Appeals Panel's Audit Guide</u>	<u>Procedures Performed</u>
Juvenile Court Schools	8	Not Applicable
Exclusion of Pupils - Pertussis Immunization	2	Yes
Class Size Reduction:		
General Requirements	7	Yes
Option One	3	Yes
Option Two	4	Not Applicable
Districts or Charter Schools With Only One School Serving K-3	4	Not Applicable
After School Education and Safety Program:		
General Requirements	4	Yes
After School	5	Yes
Before School	6	Not Applicable
Contemporaneous Records of Attendance For Charter Schools	3	Yes
Mode of Instruction for Charter Schools	1	Yes
Nonclassroom-Based Instruction/ Independent Study for Charter Schools	15	No (see below)
Determination of Funding for Nonclassroom-Based Instruction for Charter Schools	3	No (see below)
Annual Instructional Minutes - Classroom Based For Charter Schools	4	Yes

We did not perform procedures related to non-classroom based instruction at the charter schools because the non-classroom based ADA claimed by the District did not exceed the ADA threshold, which requires testing to be performed.

In our opinion, Petaluma City Schools complied, in all material respects, with the state laws and regulations referred to above for the year ended June 30, 2012, except as described in the accompanying Schedule of Findings and Questioned Costs. Further, based on our examination, for items not tested, nothing came to our attention to indicate that Petaluma City Schools had not complied, in all material respects, with state laws and regulations, except as described in the accompanying Schedule of Findings and Questioned Costs.

The District's response to the findings identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the District's Board, management, California State Controller's Office, California Department of Finance, California Department of Education, and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Stephen Roatch Accountancy Corporation

STEPHEN ROATCH ACCOUNTANCY CORPORATION
 Certified Public Accountants

March 6, 2013

STEPHEN ROATCH ACCOUNTANCY CORPORATION
Certified Public Accountants

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT
OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Board of Education
Petaluma City Schools
Petaluma, California

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Petaluma City Schools, as of and for the year ended June 30, 2012, which collectively comprise the District's basic financial statements, and have issued our report thereon dated March 6, 2013. 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.

Internal Control Over Financial Reporting

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

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings and Questioned Costs, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses, and other deficiencies that we consider to be significant deficiencies.

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. We consider certain deficiencies described in the accompanying Schedule of Findings and Questioned Costs to be material weaknesses, as noted in **Finding 12-1, 12-3, 12-4, 12-5, 12-6, 12-7, 12-8, 12-9, 12-13, 12-14, and 12-16.**

A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider certain deficiencies described in the accompanying Schedule of Findings and Questioned Costs to be significant deficiencies, as noted in **Finding 12-2, 12-10, 12-11, 12-12, 12-15, and 12-17.**

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the 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*.

The District's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of the District's Board, management, California State Controller's Office, California Department of Finance, California Department of Education, 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.

Stephen Roatch Accountancy Corporation

STEPHEN ROATCH ACCOUNTANCY CORPORATION
Certified Public Accountants

March 6, 2013

STEPHEN ROATCH ACCOUNTANCY CORPORATION
Certified Public Accountants

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

Board of Education
Petaluma City Schools
Petaluma, California

Compliance

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

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about Petaluma City Schools' 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 Petaluma City Schools' compliance with those requirements.

In our opinion, Petaluma City Schools complied, in all material respects, with the compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2012. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements, which is required to be reported in accordance with OMB Circular A-133 and which is described at **12 - 17** in the accompanying Schedule of Findings and Questioned Costs.

Internal Control Over Compliance

Management of Petaluma City Schools is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the District's internal control over compliance with the requirements that could have a direct and material effect on a major federal program 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 the District's internal control over compliance.

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

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. However, we identified a certain deficiency in internal control over compliance that we consider to be a significant deficiency as described at **12 - 17** in the accompanying Schedule of Findings and Questioned Costs. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

The District's response to the finding identified in our audit is described in the accompanying Schedule of Findings and Questioned Costs. We did not audit the response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of the District's Board, management, California State Controller's Office, California Department of Finance, California Department of Education, 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.

Stephen Roatch Accountancy Corporation

STEPHEN ROATCH ACCOUNTANCY CORPORATION
Certified Public Accountants

March 6, 2013

FINDINGS AND QUESTIONED COSTS SECTION

PETALUMA CITY SCHOOLS

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION I - SUMMARY OF AUDITOR'S RESULTS

Financial Statements

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

Material weaknesses identified?	<u> X </u>	Yes	<u> </u>	No
Significant deficiencies identified not considered to be material weaknesses?	<u> X </u>	Yes	<u> </u>	None Reported
Noncompliance material to financial statements noted?	<u> </u>	Yes	<u> X </u>	No

Federal Awards

Internal control over major programs:

Material weaknesses identified?	<u> </u>	Yes	<u> X </u>	No
Significant deficiencies identified not considered to be material weaknesses?	<u> X </u>	Yes	<u> </u>	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 Circular A-133, Section .510(a)

	<u> </u>	Yes	<u> X </u>	No
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Identification of major programs:

<u>CFDA Numbers</u>	<u>Federal Program</u>
84.410	Education Jobs Funds
84.010 / 84.377	Title I, Part A Cluster
84.367	Title II Cluster
10.553 / 10.555	Child Nutrition Cluster

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

Auditee qualified as low-risk auditee?

	<u> </u>	Yes	<u> X </u>	No
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State Awards

Internal control over state programs:

Material weaknesses identified?	<u> X </u>	Yes	<u> </u>	No
Significant deficiencies identified not considered to be material weaknesses?	<u> X </u>	Yes	<u> </u>	None Reported

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

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS

12 - 1 / 30000

MATERIAL WEAKNESS

STAFFING - INTERNAL CONTROL

Criteria: In order for districts to establish an effective system of internal control, they must provide adequate staff time to allow their employees to perform their job duties in a complete and accurate manner. In addition, they should also provide management with sufficient time to properly manage and review the work completed by the employees under their control.

Condition: The business office does not appear to be adequately staffed to provide an effective system of internal control. We noted numerous instances where business office personnel appear to be unable to perform their job duties within their contracted work day. As a result, work assignments frequently appear to be rushed and adequate work supervision does not always appear to be performed.

Questioned Costs: None.

Context: Employee positions in the business office have been reduced or eliminated, even though the responsibilities of the employees in the affected positions have continued to increase.

Effect: Many of the findings included in this audit report have likely occurred, in part, due to inadequate staffing in the business office. Although budget cuts are sometimes unavoidable, excessive budget cuts in the business office are frequently counterproductive and may actually worsen the situation for the District if the financial information provided by the business office becomes untimely or less reliable for purposes of making informed financial decisions.

Cause: Petaluma City Schools consists of two separate school districts, which share a common administration, and collectively sponsor three charter schools. As a result, the process of maintaining accounting records and preparing financial reports for Petaluma City Schools is significantly more difficult and time consuming than that of a traditional single entity school district. The District has also experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels and an increase in staff meetings. In addition, the District has recently experienced turnover in key positions, and a shortage of experienced staff who can fully utilize the overly burdensome accounting system.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

STAFFING - INTERNAL CONTROL (CONCLUDED)

Recommendation: The District should provide adequate staffing in the business office to allow their employees to perform their job duties in a complete and accurate manner. In addition, the District should also provide management with sufficient time to properly manage and review the work completed by the employees under their control.

District Response: The District was unable to secure a key position in the Business Office for the entire year. This has created a substantial burden on existing staff. The District is still in search of qualified people for this position and anticipates filling it during 2012-13.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 2 / 30000

SIGNIFICANT DEFICIENCY

AUDIT LIAISON

Criteria:

Each year, districts are provided with a comprehensive listing of the records that they will need to provide to the auditors to facilitate the timely and efficient completion of the annual audit. The listing is provided at least one month in advance of the auditor's first visit, to provide districts sufficient time to ensure that all of the required information is available in a centralized location prior to the arrival of the auditors. In order to ensure the maximum benefit of the annual audit, minimize audit fees, and limit the amount of disruption of district personnel, districts should assign an audit liaison who will make sure that all of the requested information is accumulated and placed in a centralized location prior to the arrival of the auditors.

Condition:

The District did not assign an audit liaison to assist the auditors with the 2011-12 annual audit. Instead, the comprehensive listing was cut into pieces and distributed to the various departments that were responsible for providing the requested records. Once the listing was distributed, very little follow-up was performed to ensure that the requested information would be available from the various departments, and ultimately, only a small portion of the information requested in the comprehensive listing was gathered and placed in a centralized location prior to the arrival of the auditors.

Questioned Costs:

None.

Context:

The total number of hours incurred by the auditors to complete the 2011-12 annual audit was more than double the amount of hours normally required for a district of this size and complexity. Although a large portion of the extra hours incurred were related to the correction of prior year errors, a significant portion of the excess hours were directly related to the absence of an assigned audit liaison.

Effect:

The audit process is significantly hampered when required records are not available during the auditor's visit. Accordingly, a significant amount of auditor time was spent trying to locate records to audit versus time spent actually auditing the records. Due to the District's inability to provide certain information in a timely manner, the California State Controller's Office approved an extension request allowing the District to submit its annual audit by January 31, 2013, a date which still could not be met due to a lack of available records. In addition, the auditors found it necessary to increase the audit fee to compensate for the significant unexpected complications encountered during the audit.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

AUDIT LIAISON (CONCLUDED)

Cause: The District has experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. The District has also experienced turnover in key positions, which has further hampered District employees from providing all of the information that is required to complete the annual audit in a timely manner.

Recommendation: In order to ensure the maximum benefit of the annual audit, minimize audit fees, and limit the amount of disruption of District personnel, the District should add additional staff time that would allow one individual to serve as an audit liaison. At a minimum, the audit liaison should be responsible for:

- Coordinating the scheduling of audit fieldwork dates.
- Distributing the "Client Assistance Check-List" provided by the auditors to the appropriate departments that are responsible for providing the requested records.
- Providing appropriate follow-up to ensure that all of the requested records have been prepared prior to the arrival of the auditors.
- Ensuring that all required personnel will be available for inquiries during the audit visit.
- Gathering all of the requested records from the various departments and placing them in a centralized location prior to the arrival of the auditors.
- Providing follow-up on all items that were missing or unresolved at the end of each audit visit.

District Response: The District was unable to secure a key position in the Business Office for the entire year. This has created a substantial burden on existing staff. The District is still in search of qualified people for this position and anticipates filling it during 2012-13.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 3 / 30000

MATERIAL WEAKNESS

ACCOUNTING SYSTEM

Criteria:

The financial reporting requirements of a California school district are unique and constantly changing, and the funds that are available to keep up with the reporting requirements are limited. Accordingly, districts should have an accounting system in place that is user friendly, specifically designed for school districts, and widely used throughout California. The accounting system should also be able to produce reliable financial reports that comply with applicable laws and regulations, and assist management in conducting its operations in an efficient and effective manner. In addition, the accounting system should be cost-effective, meaning that the value of the information produced should exceed the cost of producing it.

Condition:

The accounting system currently used by the District does not appear to be user friendly, specifically designed for school districts, or widely used throughout California. After several years of being on the current accounting system, District personnel are still experiencing great difficulty meeting the District's financial reporting requirements. As a result, the accounting system, as used by the District, is not always cost-effective, meaning that the value of the information produced does not exceed the cost of producing it.

Questioned Costs:

None.

Context:

Tasks that can be completed on other accounting systems with just a few keystrokes may take District personnel days or weeks to accomplish.

Effect:

District personnel appear to spend a significant amount of time and effort to compensate for the shortcomings of the accounting system. In addition, the auditors were required to wait several days to obtain certain types of financial reports that are normally produced in just a few minutes at other school districts.

Cause:

The District is the only local education agency in Sonoma County that is on the accounting system. Since the District has experienced significant turnover in key positions, there has been a shortage of experienced staff familiar enough with the accounting system to train the replacement employees. In addition, the District does not currently have any personnel that are proficient in utilizing the current accounting system to generate basic financial reports that are typically used during the audit process.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

ACCOUNTING SYSTEM (CONCLUDED)

Recommendation: The District should take appropriate steps to convert back to the accounting system maintained by Sonoma County Office of Education at the start of fiscal year 2013-14. Accordingly, the District should allocate appropriate resources to the business office to ensure that the District's fiscal year 2012-13 "Unaudited Actuals" are prepared in a complete and accurate manner to facilitate the conversion to the new accounting system.

District Response: The District is currently transitioning to the Sonoma County Office of Education financial system used by the rest of the districts in the county. The conversion will be complete for the 2013-14 fiscal year.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 4 / 30000

MATERIAL WEAKNESS

FINANCIAL REPORTING - UNAUDITED ACTUALS

Criteria: 1-2. Each year, school districts are responsible for preparing complete and accurate financial information, which is reported to the California Department of Education in the form of the "Unaudited Actuals" Financial Report. In addition, each year the governing board certifies that the report was prepared in accordance with Education Code Section 41010, and approves the report as the official submission of financial information that will be used as the basis for the District's annual financial statements. Accordingly, districts should have an effective system of internal control over financial reporting that will ensure that the information contained in the report is free of material misstatement. (In accordance with the applicable auditing standards, if material misstatements are identified during a financial audit, it is presumed that the internal control over financial reporting was either ineffective or non-existent.)

Conditions: 1. The District's internal control over financial reporting in prior years was ineffective or non-existent. As a result, the District's fiscal year 2010-11 financial statements contained several material misstatements, related to fiscal year 2010-11 and prior fiscal years, which required certain July 1, 2011 balances to be restated.

2. The District's internal control over financial reporting in the current fiscal year was ineffective or non-existent. As a result, the District's fiscal year 2011-12 "Unaudited Actuals" contained several material misstatements, related to fiscal year 2011-12, that required certain current year balances to be adjusted.

Questioned Costs: 1-2. None.

Context: 1. The restatements that were made as a result of this audit to ensure that the financial statements were fairly stated are presented on pages 49, 50, and 51 of these financial statements.

2. The adjustments that were made as a result of this audit to ensure the financial statements were fairly stated are presented on page 65 of these financial statements.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

FINANCIAL REPORTING - UNAUDITED ACTUALS (CONCLUDED)

- Effects:**
1. The fiscal year 2010-11 "Unaudited Actuals" approved by the Governing Board contained misstatements that were material to the District's annual financial statements.
 2. The fiscal year 2011-12 "Unaudited Actuals" approved by the Governing Board contained misstatements that are material to the District's annual financial statements.
- Causes:**
- 1-2. The District does not have appropriate procedures in place to ensure that the "Unaudited Actuals" financial report is free of material misstatements. In addition, the District has experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. Further, the District has also experienced turnover in key positions, which has further hampered District employees from performing up to their abilities.
- Recommendations:**
- 1-2. The District should establish appropriate procedures to ensure that the "Unaudited Actuals" financial report is free of material misstatements. The District also should provide adequate staffing in the business office to allow their employees to complete their job duties in a complete and accurate manner. In addition, the District should also provide management with sufficient time to properly manage and review the work completed by the employees under their control.
- District Responses:**
- 1-2. Due to insufficient staff and ineffective accounting system, the District was unable to provide the necessary oversight and support to meet the deadline. The District has attempted numerous recruitment efforts of qualified staff to no avail. The District is continuing its search for staff. The District is also transitioning to the Sonoma County Office of Education financial system used by the rest of the districts in the county. The conversion will be complete for the 2013-14 fiscal year.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 5 / 30000

MATERIAL WEAKNESS

REVENUE LIMIT- STATE AID

Criteria: The state aid portion of revenue limit funding is generally the District's largest source of State revenue. The determination of how much state aid should be recognized as revenue each year, is also one of the most likely places where a material misstatement of the financial statements will occur. Accordingly, the District should have procedures in place to ensure that the calculation of state aid revenue earned is reviewed in detail, and compared to prior year calculations, prior to being used as the basis for the amount of state aid reported in the "Unaudited Actuals".

Condition: The District reported state aid revenue in the "Unaudited Actuals" based on a calculation of state aid revenue earned that contained errors. As a result, the state aid portion of the District's revenue limit funding, presented in the "Unaudited Actuals" for fiscal year 2011-12 was overstated by \$263,179.

Questioned Costs: None.

Context: The overstatement accounts for less than 2% of total state aid revenue received by the District during fiscal year 2011-12.

Effect: The fiscal year 2011-12 "Unaudited Actuals" approved by the Governing Board contained a misstatement that is material to the District's annual financial statements. The adjustment that was made to ensure that the financial statements are fairly stated is presented on page 65.

Cause: The District does not have appropriate procedures in place to ensure that state aid revenue is properly computed and presented in the "Unaudited Actuals" financial report. The District has also experienced turnover in key positions, which has hampered District employees from performing up to their abilities.

Recommendations: The District should establish appropriate procedures to ensure that state aid revenue is properly computed and presented in the "Unaudited Actuals" financial report. In addition, the procedures should require that the calculation of state aid revenue earned is reviewed in detail, and compared to prior year calculations, prior to being used as the basis for the amount of state aid reported in the "Unaudited Actuals". Further, the District should provide adequate staffing in the business office to allow their employees to perform their job duties in a complete and accurate manner.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

REVENUE LIMIT- STATE AID (CONCLUDED)

District Response:

The District has had an excellent track record of being accurate. The lack of staff and an error on the spreadsheet was most of the cause of this issue. The District is continuing its search for staff. The District is also transitioning to the Sonoma County Office of Education financial system used by the rest of the districts in the county. The conversion will be complete for the 2013-14 fiscal year.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 6 / 30000

MATERIAL WEAKNESS

REVENUE RECOGNITION - CATEGORICAL PROGRAMS

Criteria: The California Department of Education (CDE) has established the Standardized Account Code Structure (SACS), which includes resource codes that are used to separately identify the various Federal and State program revenues that are allocated to districts. A current list is maintained on the CDE website, which identifies each available four digit resource code, the corresponding program name, and a "D" or "F" next to the name, which informs districts that any unspent program carryover funds are required to be reported as deferred revenue (D), or reported as a component of the ending fund balance (F). Accordingly, district procedures should require personnel to review the list on an annual basis, to ensure that all program revenues are recognized in the appropriate financial reporting period.

Condition: District personnel did not review the SACS resource code list during the year-end closing process for fiscal year 2010-11. As a result, unspent amounts received during fiscal year 2010-11, for the Education Jobs Fund program, were incorrectly reported in the prior fiscal year as revenue and a component of the ending fund balance, instead of as deferred revenue. As a result, the 2011-12 beginning fund balance of the General Fund was overstated by \$1,169,120.

Questioned Costs: None.

Context: The condition appears to have been limited to the Education Jobs Fund program.

Effect: The financial statements included in the 2010-11 audit report included a material misstatement.

Cause: The Education Jobs Fund program was a new program during fiscal year 2010-11 and the District did not determine the proper accounting treatment for the unspent program funds. The District has also experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. In addition, the District has experienced turnover in key positions, which has further hampered District employees from performing up to their abilities.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

REVENUE RECOGNITION - CATEGORICAL PROGRAMS (CONCLUDED)

Recommendation:

The District should establish appropriate procedures that require personnel to review the SACS resource code list on an annual basis, to ensure that all program revenues are recognized in the appropriate financial reporting period. The District should also provide adequate staffing in the business office to allow their employees to perform their job duties in a complete and accurate. In addition, the District should also provide management with sufficient time to properly manage and review the work completed by the employees under their control.

District Response:

The SACS software accepted it as a warning and received the following message:

CHK-RESOURCExOBJECTA - (Warning) - The following combinations for RESOURCE and OBJECT (objects 8000 through 9999, except for 9791, 9793, and 9795) are invalid. Data should be corrected or narrative must be provided explaining why the exception(s) should be considered appropriate.

EXCEPTION ACCOUNT

FD - RS - PY - GO - FN - OB RESOURCE OBJECT VALUE

01-3205-0-0000-0000-9790 3205 9790 1,169,120.44

Explanation: Did not code Ed Jobs Fund as Deferred Revenue. Since this is a Warning and the deadline was too close, the District let it remain.

The funds are fully expended and this is a non-issue.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 7 / 30000

MATERIAL WEAKNESS

REVENUE RECOGNITION - PRINCIPAL APPORTIONMENT

Criteria: Under the modified accrual basis of accounting, revenue is recorded in the fiscal year in which the resources are measurable and considered available. For programs such as supplemental instruction, gifted and talented education, community day school, and the adult education, which are funded as part of the principal apportionment, the California Department of Education (CDE) has defined "Available" as collectible within one year. Accordingly, the District should accrue current year revenue for each program up to the amounts specified on the Summary of Second Principal Apportionment.

Condition: During the prior fiscal year, the District did not accrue any revenue for amounts that had not been received by June 30, 2011, for any of the programs listed above. Accordingly, prior year revenue reported in the fiscal year 2010-11 "Unaudited Actuals" was understated by \$649,316, and current year revenue reported in the fiscal year 2011-12 "Unaudited Actuals" was overstated by \$649,316.

Questioned Costs: None.

Context: Revenue related to program amounts allocated to the District for fiscal year 2011-12 were properly accrued up to the amounts specified on the Summary of Second Principal Apportionment.

Effect: The "Unaudited Actuals" approved by the Governing Board for fiscal years 2010-11 and 2011-12, contain misstatements that are material to the District's annual financial statements.

Cause: The District does not have appropriate procedures in place to ensure that program revenues funded through the principal apportionment are recognized in the correct fiscal year. The District has experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. In addition, the District has experienced turnover in key positions, which has further hampered District employees from performing up to their abilities.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

REVENUE RECOGNITION - PRINCIPAL APPORTIONMENT (CONCLUDED)

Recommendation:

The District should establish appropriate procedures to ensure that program revenues funded through the principal apportionment are recognized in the correct fiscal year. The District should also provide adequate staffing in the business office to allow their employees to perform their job duties in a complete and accurate manner. In addition, the District should also provide management with sufficient time to properly manage and review the work completed by the employees under their control.

District Response:

The District does, in fact, have procedures. The lack of staff has been the issue.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 8 / 30000

MATERIAL WEAKNESS

BUDGET VERSUS ACTUALS

Criteria: A properly maintained budget system should accurately reflect the projected revenues, authorized expenditures, and interfund transfers of an entity. Accordingly, districts should compare the actual financial balances at year-end to the budgeted financial balances, to ensure that the recorded amounts appear consistent with the budget and are deemed appropriate prior to completing the "Unaudited Actuals".

Condition: It does not appear that the district compares the actual financial balances at year-end to the budgeted financial balances. As a result, \$278,086 of deferred maintenance apportionment revenue, which was originally deposited into the General Fund, was not transferred to the Deferred Maintenance Fund during fiscal year 2011-12, as intended by the District, and as projected in the budget. As a result, the fund balance of the General Fund was overstated by \$278,086 at June 30, 2012, and the fund balance of the Deferred Maintenance fund was understated by \$278,086.

Questioned Costs: None.

Context: The condition appears to be limited to the General Fund and Deferred Maintenance Fund.

Effect: The financial statements presented in the "Unaudited Actuals" that were approved by the Board contained errors that were material to the financial statements of the District. The adjustments that were made to ensure that the financial statements are fairly stated are presented on page 65.

Cause: The District does not have appropriate procedures in place to ensure that the recorded balances appear consistent with the budgeted balances, prior to completing the "Unaudited Actuals". The District has also experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. In addition, the District has experienced turnover in key positions, which has further hampered District employees from performing up to their abilities.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

BUDGET VERSUS ACTUALS (CONCLUDED)

Recommendation:

The District should establish appropriate procedures to ensure that the recorded balances appear consistent with the budgeted balances, prior to completing the "Unaudited Actuals". The District should also provide adequate staffing in the business office to allow their employees to perform their job duties in a complete and accurate manner. In addition, the District should also provide management with sufficient time to properly manage and review the work completed by the employees under their control.

District Response:

The District does, in fact, have procedures. The lack of staff has been the issue as well as all of the additional accounting required since the categorical funds became flexible. The General Fund transfer to Deferred Maintenance will be transferred during the 2012-13 Second Interim report.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 9 / 30000

MATERIAL WEAKNESS

EXPENDITURE RECOGNITION

Criteria: Under the modified accrual basis of accounting, expenditures are generally recognized in the accounting period in which the related fund liability is incurred, regardless of when the related invoices or progress billings are actually received. Accordingly, districts should have effective procedures in place to ensure that all significant expenditures are recorded in the appropriate financial reporting period.

Condition: The District does not currently have appropriate procedures in place to ensure that all significant expenditures, related to facilities projects, are recorded in the appropriate financial reporting period. As a result, the 2011-12 "Unaudited Actuals" Financial and Budget Report, prepared by the District, did not include \$305,670 of expenditures related to paving and roofing projects that were incurred during the current fiscal year.

Questioned Costs: None.

Context: The expenditures that were not recorded were not billed until the end of the fiscal year or slightly after the end of the year.

Effect: The financial statements presented in the "Unaudited Actuals" that were approved by the Board contained errors that were material to the financial statements of the District. The adjustment that was made to ensure that the financial statements are fairly stated is presented on page 65.

Cause: The District's current procedures do not adequately ensure that all significant expenditures, including those related to facilities projects, are recorded in the appropriate financial reporting period.

Recommendation: The District should establish appropriate procedures to ensure that all significant expenditures, including those related to facilities projects, are recorded in the appropriate financial reporting period.

District Response: The District does have specific closing criteria. The work was not scheduled to occur until 2012-13. With furlough days, the school year ended in May. The contractor was available and began the work and completed it sooner than expected. Since the budget was available and the invoice was dated in 2012-13, the invoice was paid in 2012-13. The District will remind staff to 1) verify date of completion and/or 2) have staff request a budget adjustment in the appropriate year and/or 3) have work performed when scheduled.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 10 / 30000

SIGNIFICANT DEFICIENCY

COMMERCIAL BANK ACCOUNTS

Criteria: All commercial bank accounts maintained by the District should be reconciled on a monthly basis, and the check register should be maintained on a current basis to account for all deposits and payments processed. In addition, all bank accounts should be available for audit purposes no later than the auditor's year-end visit to the District.

Condition: The District was unable to provide bank reconciliations and check registers for many of the commercial bank accounts selected for audit testing, until after the auditors had concluded their year-end visit to the District.

Questioned Costs: None.

Context: Some of the requested information was not made available until January 2013.

Effects: The lack of available commercial bank account records at the time of the auditors year-end visit to the District hampers the performance of audit procedures and impedes the auditor's ability to complete the audit by the required due date.

Cause: The District has not established appropriate procedures to ensure that complete commercial bank account records are available for audit purposes no later than the auditor's year-end visit to the District. The District has also experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. In addition, the District has experienced turnover in key positions, which has further hampered District employees from performing their duties in a timely manner.

Recommendation: The District should establish appropriate procedures to ensure that complete commercial bank account records are available for audit purposes no later than the auditor's year-end visit to the District. The District should also provide adequate staffing in the business office to allow employees to perform their job duties in a timely manner.

District Response: The District was unable to secure a key position in the Business Office for the entire year. This has created a substantial burden on existing staff to accomplish the work on a vacant desk. The District is still in search of qualified people for this position and anticipates filling it during 2012-13.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 11 / 30000

SIGNIFICANT DEFICIENCY

EXTERNAL ACCOUNTS

Criteria: All financial activity and balances related to external cash and/or investment accounts maintained by the District should be reflected on the general ledger at the appropriate amounts.

Condition: The financial activity and account balances related to two external bank accounts, was not properly reflected on the general ledger during fiscal year 2011-12.

Questioned Costs: None.

Context: One account balance was overstated by \$21,468, and the other was understated by \$4,548. Both of the misstatements are material to the funds where the balances were recorded.

Effect: The fiscal year 2011-12 "Unaudited Actuals" approved by the Governing Board contained misstatements that are material to the District's annual financial statements. The adjustments that were made to ensure that the financial statements are fairly stated are presented on page 65.

Cause: The District has not established appropriate procedures to ensure that all financial activity and balances, related to external cash and/or investment accounts maintained by the District, are properly reflected on the general ledger at the appropriate amounts. The District has also experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. In addition, the District has experienced turnover in key positions, which has further hampered District employees from performing up to their abilities.

Recommendation: The District should establish appropriate procedures to ensure that all financial activity and balances, related to external cash and/or investment accounts maintained by the District, are properly reflected on the general ledger at the appropriate amounts. The District should also provide adequate staffing in the business office to allow their employees to perform their job duties in a complete and accurate manner. In addition, the District should also provide management with sufficient time to properly manage and review the work completed by the employees under their control.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

EXTERNAL ACCOUNTS (CONCLUDED)

District Response:

Two accounts were affected; 1) Certificates of Participation (COPs) trustee account and 2) The Schwobeda Scholarship fund.

1) The COPs charges a significantly higher interest rate on approximately 14+ days prior to the due date as an 'estimate'. When the actual rates are known, the difference resides in the account under the District's name until the next payment is due. The District was not aware of the exact amount to record when the Unaudited Actuals were being prepared. In the future, the District will contact the bank to obtain this amount during closing in the future.

2) The Schwobeda Scholarship account was behind due to staffing issues. The lack of staff has created a substantial burden on existing staff to accomplish the work on a vacant desk. The District is still in search of qualified people for this position and anticipates filling it 2012.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 12 / 30000

SIGNIFICANT DEFICIENCY

UNINSURED CASH BALANCES

Criteria: Cash balances maintained in commercial bank accounts are generally insured by the Federal Depository Insurance Corporation (FDIC) up to \$250,000, unless additional agreements are reached between the districts and the individual financial institutions.

Condition: The amount of cash maintained in various accounts at a single financial institution, frequently exceeded the FDIC insured limit of \$250,000. In addition, the District was unable to provide evidence that a collateralization agreement had been made with the bank that would safeguard District balances in excess of \$250,000.

Questioned Costs: None.

Context: We noted instances where the District had more than \$1 million of uninsured cash balances sitting in commercial bank accounts at a single financial institution, at various times during fiscal year 2011-12.

Effect: The District is exposed to unnecessary risks related to maintaining uninsured cash balances in commercial bank accounts.

Cause: The District has not taken action to obtain collateralization agreements with the bank to insure balances maintained in accounts in excess of the FDIC insured amount.

Recommendation: The District should contact the bank and obtain a collateralization agreement to insure balances maintained in commercial bank accounts in excess of the FDIC insured amount.

District Response: The District has already contacted the bank regarding this issue. The collateralization agreement was delayed due to a bank merger. This process will be completed within 2012-13.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 13 / 30000

MATERIAL WEAKNESS

ACCRUAL BALANCES

Criteria: During the year, all accounts receivable and accounts payable accruals that were established in the prior year fiscal year should be reconciled to the amounts actually received or paid. If any differences are noted, the balances should be cleared from the asset and liability accounts, to the corresponding revenue and expenditure accounts, or reestablished, if appropriate. In addition, districts should be able to readily provide a detailed list of the specific items that make up the accounts receivable and accounts payable balances as of June 30 of each fiscal year, especially when districts are in the process of converting to a new accounting system.

Condition: The District was unable to provide a detailed financial report from its current accounting system that specifically identifies the individual items that make up the accounts receivable and accounts payable balances as of June 30, 2012. In addition, the District did not maintain a comprehensive listing outside of the accounting system, which specifically identifies the individual items that make up the accounts receivable and accounts payable balances as of June 30, 2012. As a result, it is extremely difficult to ascertain that the prior year accrual balances were properly cleared, and current year revenues and expenditures are properly reported.

Questioned Costs: None.

Context: The condition most adversely affected the General Fund.

Effect: If appropriate records are not prepared at the end of fiscal year 2012-13, it will make the 2013-14 accounting system conversion much more difficult.

Cause: District personnel have been overwhelmed by the effects of staff reductions and employee turnover in key positions. In addition, the District does not have any employees that are truly proficient at generating meaningful reports from the current accounting system.

Recommendation: The District should provide additional staff time to ensure that appropriate records are prepared at the end of fiscal year 2012-13, which will facilitate an easier transition into the new accounting system and provide for a more efficient annual audit.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

ACCRUAL BALANCES (CONCLUDED)

District Response:

Since the District will rely on the current financial system for the 2012-13 fiscal year, the District will contact the software provider to find the appropriate report option. The District will be utilizing the SCOE financial system effective July 1, 2013 for future reporting.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 14 / 30000

MATERIAL WEAKNESS

CLEARING ACCOUNTS

Criteria: An appropriate system of internal control over financial reporting requires that clearing accounts that are used to facilitate the payment of employee benefits, taxes, and insurance, should be reconciled on a monthly basis, to ensure that the appropriate amount of liabilities and expenditures are properly recorded.

Condition: It does not appear that the District reconciled its clearing accounts on a monthly basis or at year-end, during fiscal year 2011-12. As a result, several of the liability clearing account balances included material misstatements at June 30, 2012, as follows:

Liability Overstatements:

State Disability Insurance	\$ 1,400,405
Medicare	119,308

Liability Understatements:

Federal Income Tax Withholding	(1,400,405)
State Income Tax Liability	(119,308)

Questioned Costs: None.

Context: The condition appears to have been limited to fiscal year 2011-12.

Effect: The net effect of the overstatements/understatements of the above account balances has no impact on the current year financial statements since the balances net to zero. However, when an appropriate system of internal control over financial reporting is not in place, 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.

Cause: The District does not have appropriate procedures in place to ensure that clearing accounts, which are used to facilitate the payment of employee benefits, taxes, and insurance, are reconciled on a monthly basis. In addition, the District has also experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. Further, the District has experienced turnover in key positions, which has further hampered District employees from performing up to their abilities.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

CLEARING ACCOUNTS (CONCLUDED)

Recommendation:

The District should establish appropriate procedures to ensure that clearing accounts, which are used to facilitate the payment of employee benefits, taxes, and insurance, are reconciled on a monthly basis. The District should also provide adequate staffing in the business office to allow their employees to perform their job duties in a complete and accurate manner. In addition, the District should also provide management with sufficient time to properly manage and review the work completed by the employees under their control. Further, the balances of the four misstated accounts should be adjusted during fiscal year 2012-13 to ensure that each account properly reflects the correct balance.

District Response:

The District processes payroll and exports the file to the SCOE financial system crediting the respective liability accounts utilizing the District payroll account codes. SCOE then pays all District payroll liabilities and the District imports the resulting debits. The imports back from SCOE were in different accounts than the District. The District has reported this to SCOE and is being corrected. The review and reconciliation process would have been observed sooner had the District had the vacant position filled.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 15 / 30000

SIGNIFICANT DEFICIENCY

CAPITAL ASSETS

Criteria:

In accordance with Governmental Accounting Standards Board (GASB) Statement 34, all school districts are required to capitalize and depreciate all exhaustible capital assets in the district-wide financial statements. As a result, all school districts should have a capital asset system in place to ensure that the required capital asset information is current, accurate, and complete, and available for the auditors to examine during their year-end visit to the District.

At a minimum, capital asset systems should provide the following:

- A detailed listing of all capital assets owned by the district at the beginning of the year, which includes the historical cost and accumulated depreciation for each individual asset.
- A detailed schedule of work-in-progress at the beginning of the year, which identifies inception to date costs for each individual asset.
- A detailed listing of all current year capital asset additions, which identifies the individual assets purchased or constructed, along with the value assigned to each individual asset for purposes of capitalizing and depreciating individual assets.
- A detailed listing of all current year capital asset dispositions, which identifies the individual assets that were discarded or sold, along with the amount of sales proceeds received, if any, for purposes of computing gains and losses.
- A detailed listing of all capital assets, along with the calculation of current year depreciation expense for each individual asset.
- A detailed listing of all capital assets owned by the district at the end of the fiscal year, which includes the historical cost and accumulated depreciation for each individual asset.
- A detailed schedule of work-in-progress at the end of the year, which identifies inception to date costs for each individual asset.
- A reconciliation of current year capital outlay expenditures and facilities acquisition and construction expenditures to the capital asset inventory records.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

CAPITAL ASSETS (CONCLUDED)

Condition: Capital asset records for fiscal year 2011-12 were not available during the auditor's year-end visit to the District.

Questioned Costs: None.

Context: The audit of the District's capital asset records could not be completed until February 2013.

Effect: The lack of available capital asset records at the time of the auditors year-end visit to the District hampers the performance of audit procedures and impedes the auditor's ability to complete the audit by the required due date.

Cause: The District does not have appropriate procedures in place to ensure that all of the required capital asset information is available to be audited during the auditor's year-end visit to the District. The District has also experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. In addition, the District has experienced turnover in key positions, which has further hampered District employees from performing up to their abilities.

Recommendation: The District should establish appropriate procedures to ensure that all of the required capital asset information is available to be audited during the auditor's year-end visit to the District. The District should also provide adequate staffing in the business office to allow their employees to perform their job duties in a complete and accurate manner. In addition, the District should also provide management with sufficient time to properly manage and review the work completed by the employees under their control.

District Response: This issue is not due to lack of procedures or understanding of the requirements associated with this finding. When provided, the records were 100% accurate and complete. The District was unable to secure a key position in the Business Office for the entire year. This has created a substantial burden on existing staff to accomplish the work on a vacant desk. The District is still in search of a qualified people for this position and anticipates filling it during 2012-13.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONTINUED)

12 - 16 / 30000

MATERIAL WEAKNESS

GENERAL OBLIGATION BONDS

Criteria: The financial statement balances related to a district's outstanding general obligation bonds, are generally some of the largest balances presented in the government-wide statement of net assets. Accordingly, having an effective system of internal control over financial reporting requires district's to have appropriate procedures in place to ensure that the liability balances presented are current, accurate and complete.

Condition: The District does not currently have effective procedures in place to ensure that the financial statement balances, presented in the government-wide statement of net assets, related to the District's outstanding general obligation bonds, are current, accurate and complete. As a result, the District relied solely upon the work of the previous audit firm to ensure that the balances were fairly stated; however, it has since been discovered that the prior year balances, related to the District's outstanding bond obligations, which were presented in the prior year audit report, contained several material misstatements. As a result, beginning net asset balance presented in this financial statement has been restated, as discussed in Note 22.

Questioned Costs: None.

Context: The account balances related to the District's outstanding general obligation bonds were misstated as follows:

- The prior year liability reported for outstanding general obligation bonds was overstated by \$4,826,042, due to the inclusion of liabilities related to two separate bond issues that were defeased in prior fiscal years, but never removed as liabilities of the District.
- The prior year liability reported for unamortized bond premiums was understated by \$92,295, due to accounting errors related to prior year bond refunding transactions.
- The prior year asset balance for unamortized bond issuance costs was overstated by \$691,601, due to accounting errors related to prior year bond refunding transactions.
- The prior year asset balance for unamortized bond refunding costs was understated by \$1,187,510, due to accounting errors related to prior year bond refunding transactions.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION II - FINANCIAL STATEMENT FINDINGS (CONCLUDED)

GENERAL OBLIGATION BONDS (CONCLUDED)

Effect: When appropriate procedures are not in place to ensure that all financial statement balances, related to general obligation bond transactions, are current, accurate, and complete, there is a reasonable possibility that a material misstatement of the District's financial statements will not be prevented, detected or corrected in a timely manner.

Cause: Due to the complex nature of certain bond related transactions, districts typically rely on the work of the independent auditors to determine the bond related balances that should be presented in their financial statements. The District has also experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. In addition, the District has experienced turnover in key positions, which has further hampered District employees from performing up to their abilities.

Recommendation: The District should establish appropriate procedures to ensure that all bond related financial statement balances are current, accurate, and complete. In addition, although it is fine to request auditor assistance in determining the financial statement balances, District personnel should never rely solely on the work of the auditor until they fully understand the financial transaction and agree with the reported balances. The District should also provide adequate staffing in the business office to allow their employees to perform their job duties in a complete and accurate manner. In addition, the District should also provide management with sufficient time to properly manage and review the work completed by the employees under their control.

District Response: The District staff will analyze the bond transactions to ensure they are accurate. If balances are not in agreement with what the auditor suggests, there will be a review until the differences are ascertained and consensus is reached.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

12 - 17 / 50000 / 30000

SIGNIFICANT DEFICIENCY

U.S. Department of Education
Passed through California Department of Education

Education Jobs Funds: CFDA 84.410 (2010-11 annual audit reported during fiscal year 2011-12)

DATA COLLECTION FORM

- Criteria:**
1. In accordance with OMB Circular A-133 and OMB Memorandum M-10-14, districts that are required to be audited under the Single Audit Act must submit the Data Collection Form within 30 days of the date the auditor releases the audit report, or 9 months after the end of the audit period, whichever date occurs first. Accordingly, districts should have appropriate procedures in place to ensure that the Data Collection form is submitted by the required due date. (The Data Collection Form prepared for the District's 2010-11 audit report was due to be submitted to the Federal Audit Clearinghouse no later than January 14, 2012.)
 2. In accordance with the Data Collection Form instructions, districts are required to sign an Auditee Certification Statement, which states in part that, to the best of my knowledge and belief, the information presented in the Data Collection Form, including the schedule of Federal Awards Expended, is accurate and complete. Accordingly, districts should have appropriate procedures in place to ensure that the information presented in the Data Collection Form is verified prior to signing the Auditee Certification Statement.
- Conditions:**
1. The Data Collection Form prepared for the District's 2010-11 audit report was not submitted to the Federal Audit Clearinghouse until January 2013.
 2. The Data Collection Form prepared for the District's 2010-11 audit report agreed to the information presented in the audit report, but the amount reported as being expended from the Education Jobs Fund program in the 2010-11 audit report and Data Collection Form, did not agree to the District's general ledger.
- Questioned Costs:**
- 1-2. None. There is no fiscal impact associated with this finding.
- Context:**
1. The Data Collection Form was submitted approximately one-year after the required due date.
 2. The amount of expenditures reported in the 2010-11 audit report and the related Data Collection Form, for the Education Jobs Fund program, was overstated by \$1,169,120.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS (CONCLUDED)

DATA COLLECTION FORM (CONCLUDED)

- Effects:
1. If the District was not already considered a high-risk auditee, the District would have lost its low-risk auditee status for two years, which would have resulted in the need for additional federal programs to be tested and a corresponding increase in audit fees.
 2. The District did not detect the error in the 2010-11 audit report or the Data Collection Form, and improperly certified information that was inaccurate.
- Causes:
1. The District did not have adequate procedures in place to ensure that the Data Collection Form was filed by the required due date.
 2. District personnel did not perform a detailed review of the 2010-11 audit report or Data Collection Form and relied solely on the information provided by the previous auditors.
- Recommendations:
1. The District should establish appropriate procedures to ensure that future Data Collection Forms are filed by the required due dates.
 2. The District should establish procedures that require future audit reports and data collection forms to be reviewed in detail prior to being approved or certified.
- District Responses:
1. With regard to the OMB data submission, the District will ensure the deadline is not missed.
 2. With regard to the Ed Jobs Fund, as indicated in finding 12-6, the error was not fatal. Whether the revenue was 'deferred' or held as part of a restricted ending balance, the unspent remaining amount of the entitlement from 2010-11 was correct and the District fully expended the amount in 2011-12. The issue is strictly a 're-class' of resources that were rightfully available to the District.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS

12 - 18 / 10000 / 40000

MATERIAL WEAKNESS

REVENUE LIMIT REPORTING

Criteria: In accordance with Education Code Section 42238.5, districts receive funding based on the second principal apportionment regular average daily attendance (ADA) for either the current or prior fiscal year, whichever is greater. In addition, in accordance with Education Code Section 42238.51, the prior fiscal year ADA, mentioned above, must be reduced by the ADA of pupils who attended a non-charter school of the District in the prior fiscal year, and who attended a charter school sponsored by the District in current year. (On an individual pupil basis, the amount of the prior year reduction cannot exceed the attendance claimed for the pupil by the charter school in the current year.)

Condition: In the revenue limit reporting software, the District did not report the correct average daily attendance (ADA) for pupils who attended a non-charter school of the District in fiscal year 2010-11 and who attended a charter school sponsored by the District in fiscal year 2011-12. As a result, prior year P-2 ADA, reported for the Petaluma City Elementary School District, in the revenue limit reporting software was overstated by 56.56 ADA, which resulted in prior year average daily attendance of 2,089.53 ADA, which is 8.63 ADA higher than 2011-12 P-2 average daily attendance of 2,080.90 ADA.

Questioned Costs: \$42,522. (8.63 Disallowed P-2 ADA X 4,927.22 Deficited Per ADA Base Revenue Limit)

Context: The District opened the 6th Grade Academy Charter School during fiscal year 2011-12, but did not adjust prior year P-2 ADA, as required by Education Code Section 42238.51.

Effect: If the adjustment is not made, the District will have been paid twice for the same 8.63 ADA. The District received funding through the general purpose block grant and the revenue limit.

Cause: District personnel were unaware that the prior year ADA needed to be entered manually into the revenue limit software in order to comply with the requirements of Education Code Section 42238.51.

Recommendation: The District should report 56.56 ADA in the space on the 2011-12 P-2 revenue limit reporting software that has been designated for pupils who attended a non-charter school of the District in fiscal year 2010-11 and who attended a charter school sponsored by the District in fiscal year 2011-12.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS (CONTINUED)

REVENUE LIMIT REPORTING (CONCLUDED)

District Response:

The P-2 Revenue Limit form will be submitted for correction. The District will review with staff the protocol for potential ADA impact when a new charter school is implemented.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS (CONTINUED)

12 - 19 / 10000

SIGNIFICANT DEFICIENCY

KINDERGARTEN CONTINUANCE

Criteria: Education Code Section 46300(g) allows a district to include in its average daily attendance kindergarten pupils who have already completed one school year in kindergarten only if the school district has on file for each of those pupils an agreement made pursuant to Education Code Section 48011, approved in form and content by the California Department of Education (CDE), and signed by the pupil's parent or guardian near the anniversary date of the pupil's kindergarten admittance.

Condition: During fiscal year 2011-12, the District allowed two (2) kindergarten students to attend a second year of kindergarten, prior to obtaining agreements made pursuant to 48011 that were approved in form and content by the CDE. As a result, the average daily attendance (ADA) reported on the P-2 and Annual attendance reports for fiscal year 2011-12 was overstated by 0.79 ADA and 1.03 ADA, respectively.

Questioned Costs: \$3,893. (0.79 Disallowed P-2 ADA X 4,927.22 Deficited Per ADA Base Revenue Limit)

Context: The condition appears to be limited to Grant Elementary School.

Effect: The District did not comply with the requirements of Education Code Section 48011.

Cause: The state compliant kindergarten continuance form provided by the Business Office was not used.

Recommendation: The District should establish procedures to ensure that state compliant kindergarten continuance forms are used at all elementary school sites. (Since the most recent P-2 and Annual attendance reports have been submitted with the disallowed ADA omitted, no further action is required.)

District Response: The District will provide training and proper/current forms to elementary principals. As noted by the auditor, the 2011-12 P-2 and Annual corrective reports have already been submitted.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS (CONTINUED)

12 - 20 / 40000

SIGNIFICANT DEFICIENCY

AFTER SCHOOL EDUCATION AND SAFETY PROGRAM

- Criteria: 1-2. In accordance with Education Code Section 8483 (a)(2), it is the intent of the Legislature that elementary school pupils attend the entire program every day that the program operates, with the exception of absences allowed under each district's early release policy. In addition, Education Code Section 8483 (a)(3), requires districts to give enrollment priority to students who are able to attend the program daily. Accordingly, districts must have a system in place to classify student absences, as either allowable or unallowable in accordance with the district's early release policy, and must be able to utilize such data to ensure that the students, who are able to attend the program the most, are given enrollment priority over those students who are unable to attend.
- Conditions: 1-2. The District has contracted with the Boys & Girls Clubs of Marin and Southern Sonoma Counties, to fulfill the requirements of providing afterschool services at the McKinley and McDowell Elementary Schools. The contractor has developed appropriate records, for classifying student absences as either allowable or unallowable in accordance with the district's early release policy; however, the contractor has not established appropriate procedures to ensure that the attendance sign in/out sheets are being completed in accordance with the intent of the form. As a result, we noted numerous instances where students were released from the program and the designated space provided for the early release reason code was left blank or filled in with an invalid code.
- Questioned Costs: 1-2. None. The District's failure to use early release codes as a means of prioritizing student enrollment in the program does not affect program attendance, and has no fiscal impact on District funding.
- Context: 1. Of the 388 days of attendance tested at McDowell Elementary 362 of the days did not properly include a valid early release code to identify the reason for the absence.
2. Of the 326 days of attendance tested at McKinley Elementary 87 of the days did not properly include a valid early release code to identify the reason for the absence.
- Effects: 1-2. The District does not appear to have appropriate procedures in place to ensure compliance with Education Code Sections 8483 (a)(2) and 8483 (a)(3) .

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS (CONTINUED)

AFTER SCHOOL EDUCATION AND SAFETY PROGRAM (CONCLUDED)

- Causes: 1-2. The District has not established appropriate procedures to review the attendance records that are prepared and maintained by the contractor.
- Recommendations: 1-2. The District should establish appropriate procedures to review the attendance records that are prepared and maintained by the contractor, to ensure that the program is operated in accordance with state laws.
- District Responses: 1-2. The early release issue has been addressed by the District with the Boys & Girls Club in previous years. The District will investigate the procedures utilized by the Boys & Girls Club to have corrective action implemented immediately. The District will ensure that staff are trained to review attendance records for completeness and accuracy, including compliance with early release requirements.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS (CONTINUED)

12 - 21 / 72000

SIGNIFICANT DEFICIENCY

SCHOOL ACCOUNTABILITY REPORT CARD

<u>Criteria:</u>	On November 8, 1988, California voters passed Proposition 98, also known as <i>The Classroom Instructional Improvement and Accountability Act</i> . This ballot initiative provides California public schools with a stable source of funding. In return, all public schools in California are required to prepare school accountability report cards on an annual basis and disseminate them to the public by February 1.
<u>Condition:</u>	The school accountability report cards that were required to be prepared and disseminated to the public by February 1, 2012, were not available on the District website until the end of October 2012.
<u>Questioned Costs:</u>	None.
<u>Context:</u>	The school accountability report cards were posted to the district website approximately nine months after the February 1 due date.
<u>Effect:</u>	The District did not comply with the requirements of Proposition 98, and the information contained in the various school accountability report cards was not disseminated to the general public until October 2012.
<u>Cause:</u>	The District has not established appropriate procedures to ensure that all school accountability report cards have been prepared and disseminated to the public by February 1 of each year.
<u>Recommendation:</u>	The District should establish appropriate procedures to ensure that all school accountability report cards are prepared and disseminated to the public by February 1 of each year.
<u>District Response:</u>	The delay in posting SARC data is a result of funding cuts and resultant staff reductions. The cuts at the State level have pushed other reporting duties and constant changes onto Districts to manage. As funding is restored, The District will add back staff. However, the District priorities are to restore student days back to 180 and provide certificated staff development. The District will make every effort to meet the deadline in the future.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS (CONTINUED)

12 - 22 / 40000

SIGNIFICANT DEFICIENCY

INCENTIVES FOR LONGER INSTRUCTIONAL DAY

<u>Criteria:</u>	Annually, districts receive incentive funding for increasing instructional time as provided by the Incentives for Longer Instructional Day. As a result, the auditors are required to verify the district's calculation of instructional minutes, for each school in the district, and agree the information in the calculation to the school calendars and bell schedules that support each calculation. Accordingly, districts should establish appropriate procedures to ensure that all bell schedules and school calendars used to prepare the various instructional minute calculations are retained and provided to the auditor at the beginning of the audit.
<u>Condition:</u>	The instructional minute calculations prepared by the District for fiscal year 2011-12, were not always supported by bell schedules or school calendars. As a result, supporting documentation had to be requested from the various school sites, who subsequently provided the missing information over a period of days.
<u>Questioned Costs:</u>	None. Once all records were available, it was determined that all sites provided at least the minimum required number of instructional minutes.
<u>Context:</u>	The condition was most prevalent for bell schedules related to shortened school days that were not always identified on school calendars.
<u>Effect:</u>	The audit of instructional minutes could not be completed in a timely manner due to the lack of readily available supporting documentation.
<u>Cause:</u>	The District has not established appropriate procedures to ensure all instructional minute calculations, provided to the auditors, are supported by the bell schedules and school calendars that were used to prepare the calculations.
<u>Recommendation:</u>	The District should establish appropriate procedures to ensure all instructional minute calculations, provided to the auditors, are supported by the bell schedules and school calendars that were used to prepare the calculations.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS (CONTINUED)

INCENTIVES FOR LONGER INSTRUCTIONAL DAY (CONCLUDED)

District Response:

The District currently has requirements for the sites to submit their bell schedules for the year and calculation of instructional minutes to the District Office. The District will investigate the cause of the delay in accessing information and will establish and implement any necessary procedures to ensure sites have the bell schedule in order and available.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS (CONTINUED)

12 - 23 / 40000

SIGNIFICANT DEFICIENCY

FINANCIAL REPORTING DEADLINE

<u>Criteria:</u>	Education Code Section 42100 requires the governing board of each school district to approve the "Unaudited Actuals" financial report on or before September 15 th following the close of the fiscal year.
<u>Condition:</u>	The District did not provide the 2011-12 "Unaudited Actuals" financial report to the governing board for approval, until September 25, 2012.
<u>Questioned Costs:</u>	None.
<u>Context:</u>	The "Unaudited Actuals" financial report was approved 10 days late but was noticeably prepared in a rushed and incomplete manner.
<u>Effect:</u>	The District did not comply with the requirements of Education Code Section 42100, and the final "Unaudited Actuals" contained several errors, which did not reflect the true capabilities of the employees who prepared them.
<u>Cause:</u>	Petaluma City Schools consists of two separate school districts that share a common administration, that collectively sponsor three charter schools. As a result, the process of maintaining accounting records and preparing financial reports for Petaluma City Schools is significantly more difficult and time consuming than that of a traditional single entity school district. In addition, the District has experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. The District has also experienced turnover in key positions, and a shortage of experienced staff that can fully utilize the current overly burdensome accounting system.
<u>Recommendation:</u>	The District should provide adequate staff time in the business office to ensure that all employees have sufficient time to perform their job duties in a complete and accurate manner. In addition, the District should provide management with sufficient time to manage and review the work completed by the employees under their control.
<u>District Response:</u>	The District was unable to secure a key position in the Business Office for the entire year. This has created a substantial burden on existing staff to accomplish the work on a vacant desk. The District is still in search of qualified people for this position and anticipates filling it during 2012-13. The District has in the past and will make every effort to meet deadlines.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS (CONTINUED)

12 - 24 / 40000

MATERIAL WEAKNESS

FINANCIAL REPORTING - PRIOR YEAR AUDIT ADJUSTMENTS

Criteria: In accordance with Education Code Section 41010, the accounting records of all school districts shall be maintained in accordance with the procedures published in the California School Accounting Manual. Accordingly, school districts are required to record adjustments in the current year general ledger to reflect the audit adjustments presented in the prior year audit report. In addition, the effect of the adjustment on the prior year ending fund balance should be recorded in the general ledger in Object 9793, which will automatically upload into the appropriate place in the "Unaudited Actuals" financial report.

Condition: No adjustments were made in the current year general ledger to reflect the audit adjustments included in the prior year audit report, that were related to the Enterprise Fund (Downtown Project Fund). As a result, the beginning balance of the Enterprise Fund, presented in the 2011-12 "Unaudited Actuals" financial report, did not agree to the ending fund balance presented in the prior year audit report.

Questioned Costs: None.

Context: The beginning fund balance of the Enterprise Fund, presented in the 2011-12 "Unaudited Actuals" financial report was understated by \$29,841.

Effect: The financial statements presented in the "Unaudited Actuals" that were approved by the Board contain errors that are material to the financial statements of the District, which required current year audit adjustments.

Cause: The District has not established appropriate procedures to ensure that the beginning fund balances presented in the "Unaudited Financials" financial report agree to the balances presented in the prior year audit report. The District has also experienced a significant decline in funding due to the effects of a recessionary economy, which has resulted in reduced staffing levels. In addition, the District has experienced turnover in key positions, which has further hampered District employees from performing up to their abilities.

PETALUMA CITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

SECTION IV - STATE AWARD FINDINGS AND QUESTIONED COSTS (CONCLUDED)

FINANCIAL REPORTING - PRIOR YEAR AUDIT ADJUSTMENTS (CONCLUDED)

Recommendation:

The District should establish appropriate procedures to ensure that the beginning fund balances presented in the "Unaudited Financials" financial report, agree to the balances presented in the prior year audit report. The District should also provide adequate staffing in the business office to allow employees to perform their job duties in a complete and accurate manner. In addition, they should also provide management with sufficient time to properly manage and review the work completed by the employees under their control.

District Response:

The District will implement procedures to ensure that audit adjustments are posted.

PETALUMA CITY SCHOOLS
STATUS OF PRIOR YEAR RECOMMENDATIONS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

<u>Recommendations</u>	<u>Current Status</u>	<u>Explanation If Not Fully Implemented</u>
<u>FINANCIAL STATEMENTS</u>		
11 - 1 / 30000		
SIGNIFICANT DEFICIENCY		
<u>STUDENT BODY FUNDS</u>		
Periodic training should be provided to all individuals who are assigned responsibility for maintaining and supervising student body accounts and activities at each school site. FCMAT's student body accounting manual is available online and can be used as resource materials to supplement any ASB procedures and policies already provided to the sites.	Implemented	
11 - 2 / 30000		
SIGNIFICANT DEFICIENCY		
<u>SITE CASH AND REVOLVING FUNDS</u>		
We recommend the District remind all sites that they are responsible for ensuring that all cash collections are properly reported by pre-numbered receipts and deposited timely. Additionally, support for deposits made to the District clearing account should include a list of receipts included in the deposit as well as which general ledger accounts are expected to be credited.	Implemented	
11 - 3 / 30000		
SIGNIFICANT DEFICIENCY		
<u>DISTRICT CASH COLLECTION</u>		
We recommend that the District keep a log of all receipts including checks and site deposits noting the amount received, who it is from, and the date received. The daily receipts should be kept in a safe or other similar location out of the view of other personnel and the public until collections are deposited.	Implemented	

PETALUMA CITY SCHOOLS
STATUS OF PRIOR YEAR RECOMMENDATIONS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

<u>Recommendations</u>	<u>Current Status</u>	<u>Explanation If Not Fully Implemented</u>
<u>FINANCIAL STATEMENTS (CONCLUDED)</u>		
11 - 4 / 30000		
SIGNIFICANT DEFICIENCY		
<u>CONTROLS OVER PAYROLL TRANSACTIONS</u>		
The ability for payroll staff to change certain screens in the system should be prohibited. A review of the system segregation controls should be performed. Additionally, a manual verification of actual pay rates to the pay rates per employee contracts or salary schedules should be performed for all employees who are hired after the start of the fiscal year, have a pay rate change after the start of the fiscal year, or change positions after the start of the fiscal year.	Implemented	
11 - 5 / 30000		
SIGNIFICANT DEFICIENCY		
<u>JOURNAL ENTRIES</u>		
In order to strengthen controls over journal entries, we recommend that only certain employees have the authority to approve journal entry transactions and those same employees are not allowed to also input the journal entries into the system.	Implemented	

PETALUMA CITY SCHOOLS
STATUS OF PRIOR YEAR RECOMMENDATIONS
FOR THE FISCAL YEAR ENDED JUNE 30, 2012

<u>Recommendations</u>	<u>Current Status</u>	<u>Explanation If Not Fully Implemented</u>
<u>FEDERAL AWARDS</u>		
11 - 6 / 50000		
SIGNIFICANT DEFICIENCY		
<u>TRADITIONAL TEACHING AMERICAN HISTORY PROJECT CFDA # 84.215X</u>		
We recommend that the District establish official written policies and procedures that reference all of the federal requirements. Included in these procedures should be requirements that staff determine that entities receiving sub-awards of an value and procurement contracts equal to or exceeding \$25,000, and their principals, are not suspended or debarred, and specify the means that will be used to make the determination, i.e. checking the Excluded Parties Listing System (EPLS), obtaining a certification from the vendors or containing a clause in their agreements.	Implemented	
<u>STATE AWARDS</u>		
11 - 7 / 10000		
SIGNIFICANT DEFICIENCY		
<u>ATTENDANCE CODE</u>		
We recommend that the site print out weekly attendance rosters every week and have the site teachers review and certify the accuracy of the information.	Implemented	