
Kalamazoo Regional Educational Service Agency

**Financial Report
with Supplemental Information
June 30, 2018**

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Independent Auditor's Report

To the Board of Education
Kalamazoo Regional Educational Service Agency

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of Kalamazoo Regional Educational Service Agency (the "Agency") as of and for the year ended June 30, 2018 and the related notes to the financial statements, which collectively comprise Kalamazoo Regional Educational Service Agency's basic financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of Kalamazoo Regional Educational Service Agency as of June 30, 2018 and the respective changes in its financial position and, where applicable, cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 2 to the basic financial statements, as of July 1, 2017, the Agency adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*. The Agency's unrestricted net position has been restated as of July 1, 2017 as a result of this change in accounting principle. Our opinion is not modified with respect to this matter.

To the Board of Education
Kalamazoo Regional Educational Service Agency

Required Supplemental Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, pension system schedules of funding progress and employer contributions, and the major funds budgetary comparison schedules be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplemental information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise Kalamazoo Regional Educational Service Agency's basic financial statements. The other supplemental information, as identified in the table of contents, is presented for the purpose of additional analysis and is not a required part of the basic financial statements.

The other supplemental information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the other supplemental information is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 23, 2018 on our consideration of Kalamazoo Regional Educational Service Agency's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Kalamazoo Regional Educational Service Agency's internal control over financial reporting and compliance.



October 23, 2018

Kalamazoo Regional Educational Service Agency

Management's Discussion and Analysis

This section of Kalamazoo Regional Educational Service Agency's (the "Agency") annual financial report presents our discussion and analysis of the Agency's financial performance during the year ended June 30, 2018. Please read it in conjunction with the Agency's financial statements, which immediately follow this section.

Using this Annual Report

This annual report consists of a series of financial statements and notes to those financial statements. These statements are organized so the reader can understand Kalamazoo Regional Educational Service Agency financially as a whole. The agency-wide financial statements provide information about the activities of the whole Agency, presenting both an aggregate view of the Agency's finances and a longer-term view of those finances. The fund financial statements provide the next level of detail. For governmental activities, these statements tell how services were financed in the short term, as well as what remains for future spending. The fund financial statements look at the Agency's operations in more detail than the Agency-wide financial statements by providing information about the Agency's most significant funds - the General Fund and the Special Education Fund- as well as information on the Agency's debt service, enterprise, and internal service funds. The remaining statement, the statement of fiduciary assets and liabilities, presents financial information about activities for which the Agency acts solely as an agent for the benefit of students and parents. This report is composed of the following elements:

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

Basic Financial Statements

Agency-wide Financial Statements

Fund Financial Statements

Notes to Financial Statements

Required Supplemental Information

Budgetary Information for Major Funds

Schedules of the Agency's Proportionate Share of the Net Pension and OPEB Liabilities

Schedules of Pension and OPEB Contributions

Other Supplemental Information

Reporting the Agency as a Whole - Agency-wide Financial Statements

The statement of net position and the statement of activities, which appear first in the Agency's financial statements, report information on the Agency as a whole and its activities. We prepare these statements to include all assets, deferred outflows of resources, liabilities, and deferred inflows of resources, using the accrual basis of accounting, which is similar to the accounting used by most private sector companies. All of the current year's revenue and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Agency's net position, the difference between assets plus deferred outflows of resources and liabilities plus deferred inflows of resources, as reported in the statement of net position. The relationship between revenue and expenses is the Agency's operating results. However, the Agency's goal is to provide services to our students, not to generate profits as commercial entities do. One must consider many other nonfinancial factors, such as the quality of the education provided and the safety of the schools, to assess the overall health of the Agency.

The statement of net position and the statement of activities report the governmental activities for the Agency, which encompass all of the Agency's services, including instruction, support services, and community services. Property taxes, unrestricted state aid (foundation allowance revenue), and state and federal grants finance most of these activities.

Kalamazoo Regional Educational Service Agency

Management's Discussion and Analysis (Continued)

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

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

Governmental Funds

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

Proprietary Funds

The Agency has one enterprise fund and one internal service fund that are reported as proprietary funds. These funds are reported using the accrual basis of accounting, just as in the agency-wide statements described above.

The Agency as Trustee - Reporting the Agency's Fiduciary Responsibilities

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

Kalamazoo Regional Educational Service Agency

Management's Discussion and Analysis (Continued)

The Agency as a Whole

Recall that the statement of net position provides the perspective of the Agency as a whole. The following table provides a summary of the Agency's net position as of June 30, 2018 and 2017:

| | Governmental Activities | | Business-type Activities | |
|---------------------------------------|-------------------------|------------------|--------------------------|-----------------|
| | 2018 | 2017 | 2018 | 2017 |
| | (in millions) | | (in millions) | |
| Assets | | | | |
| Current and other assets | \$ 24.4 | \$ 23.4 | \$ 0.2 | \$ 0.2 |
| Capital assets | 27.0 | 27.6 | - | - |
| Total assets | 51.4 | 51.0 | 0.2 | 0.2 |
| Deferred Outflows of Resources | 22.7 | 13.7 | 0.4 | 0.2 |
| Liabilities | | | | |
| Current liabilities | 12.5 | 11.5 | - | 0.1 |
| Noncurrent liabilities | 9.9 | 12.3 | - | - |
| Net pension liability | 77.8 | 72.2 | 1.1 | 1.0 |
| Net OPEB liability | 26.7 | - | 0.4 | - |
| Total liabilities | 126.9 | 96.0 | 1.5 | 1.1 |
| Deferred Inflows of Resources | 8.1 | 2.5 | 0.2 | - |
| Net Position | | | | |
| Net investment in capital assets | 19.0 | 17.0 | - | - |
| Restricted | 0.3 | 0.2 | - | - |
| Unrestricted | (80.2) | (51.0) | (1.1) | (0.7) |
| Total net position | <u>\$ (60.9)</u> | <u>\$ (33.8)</u> | <u>\$ (1.1)</u> | <u>\$ (0.7)</u> |

The above analysis focuses on net position. The change in net position of the Agency's governmental activities is discussed below. The Agency's governmental net position was \$(60.9) million at June 30, 2018. Net investment in capital assets totaling \$19.0 million compares the original cost, less depreciation of the Agency's capital assets, to long-term debt used to finance the acquisition of those assets. Restricted net position is reported separately to show legal constraints from debt covenants and enabling legislation that limit the Agency's ability to use that net position for day-to-day operations. The remaining amount of governmental activities net position (\$(80.2) million) and the business-type activities net position (\$(1.2) million) was unrestricted.

The \$(80.2) million in unrestricted net position of governmental activities represents the accumulated results of all past years' operations. Without GASB Statement No. 68 and GASB Statement No. 75, total net position would be \$29.1 million. The unrestricted net position balance enables the Agency to meet working capital and cash flow requirements, as well as to provide for future uncertainties. The operating results of the General Fund will have a significant impact on the change in unrestricted net position from year to year.

Kalamazoo Regional Educational Service Agency

Management's Discussion and Analysis (Continued)

The results of this year's operations for the Agency as a whole are reported in the condensed statement of activities below, which shows the changes in net position for the years ended June 30, 2018 and 2017:

| | Governmental Activities | | Business Type Activities | |
|---|-------------------------|-------------------------|--------------------------|------------------------|
| | 2018 | 2017 | 2018 | 2017 |
| | (in millions) | | (in millions) | |
| Revenue | | | | |
| Program revenue: | | | | |
| Charges for services | \$ 6.6 | \$ 6.1 | \$ 2.3 | \$ 2.8 |
| Operating grants | 41.7 | 42.0 | - | - |
| General revenue: | | | | |
| Property taxes | 47.9 | 46.9 | - | - |
| Unrestricted state revenue | 5.9 | 4.9 | - | - |
| Other | 0.4 | 0.5 | - | - |
| Total revenue | 102.5 | 100.4 | 2.3 | 2.8 |
| Expenses | | | | |
| Instruction | 23.4 | 21.8 | - | - |
| Support services | 33.9 | 31.1 | - | - |
| Community services | 4.3 | 3.7 | - | - |
| Intergovernmental transfers | 39.7 | 39.6 | - | - |
| Interest on long-term debt | 0.2 | 0.5 | - | - |
| Depreciation (unallocated) | 1.0 | 1.1 | - | - |
| Technology services | - | - | 2.5 | 3.6 |
| Total expenses | 102.5 | 97.8 | 2.5 | 3.6 |
| Transfers | (0.2) | - | 0.2 | - |
| Change in Net Position | (0.2) | 2.6 | - | (0.8) |
| Net Position - Beginning of year, as previously stated | (33.8) | (36.4) | (0.7) | 0.1 |
| Cumulative Effect of Change in Accounting | (26.9) | - | (0.4) | - |
| Net Position - Beginning of year | (60.7) | (36.4) | (1.1) | 0.1 |
| Net Position - End of year | <u>\$ (60.9)</u> | <u>\$ (33.8)</u> | <u>\$ (1.1)</u> | <u>\$ (0.7)</u> |

As reported in the statement of activities, the cost of all of our governmental activities this year was \$102.5 million. Certain activities were partially funded from those who benefited from the programs (\$6.6 million) or by other governments and organizations that subsidized certain programs with grants and contributions (\$41.7 million). We paid for the remaining "public benefit" portion of our governmental activities with \$47.9 million in taxes, \$5.9 million in state foundation allowance, and with our other revenue (i.e., interest and general entitlements). The Agency experienced a decrease in net position of \$(0.2) million.

As reported in the statement of activities, the cost of all business-type activities this year was \$2.5 million and was funded entirely by those who benefited from the services.

As discussed above, the net cost shows the financial burden that was placed on the State and the Agency's taxpayers by each of these functions. Since property taxes for operations and unrestricted state aid constitute the vast majority of district operating revenue sources, the Board of Education and administration must annually evaluate the needs of the Agency and balance those needs with state-prescribed available unrestricted resources.

Kalamazoo Regional Educational Service Agency

Management's Discussion and Analysis (Continued)

As required by the Governmental Accounting Standards Board (GASB), the Agency adopted GASB Statement No. 75. This standard required the inclusion of the Agency's proportionate share of the Michigan Public School Employees' Retiree Health Care Plan within the Agency's financial statements, affecting July 1, 2017 beginning net position by \$27.3 million, and the inclusion of the net OPEB obligation and related deferred inflows and outflows of resources in the June 30, 2018 financial statements. All governments participating in the plan were required to adopt this new standard.

The Agency joined with other adjoining intermediate school districts to develop a technology services consortium. The business-type activities show the results for this collaborative venture. The cost of our business-type activities this year was \$2.5 million, which included the effects of the GASB Statement No. 68 and No.75 and the business-type activities proportionate share of the pension and OPEB liabilities. These activities were funded by those who benefited from the services provided (\$2.3 million) and a transfer from the Agency (\$0.2 million).

The Agency's Funds

As we noted earlier, the Agency uses funds to help it control and manage money for particular purposes. Looking at funds helps the reader consider whether the Agency is being accountable for the resources taxpayers and others provide to it and may provide more insight into the Agency's overall financial health.

As the Agency completed this year, the governmental funds reported a combined fund balance of \$10.5 million, which is a decrease of \$0.02 million from last year. General Fund fund balance is available to fund costs related to allowable agency operating purposes. The Special Education Fund fund balance is available to fund future costs related to the Agency's special education programs. The Debt Service Fund fund balance will fund future debt service payments, and the Capital Projects Funds fund balances are available to fund capital project needs within the Agency.

Budgetary Highlights

Over the course of the year, the Agency revises its budget as it attempts to deal with unexpected changes in revenue and expenditures. State law requires that the budget be amended to ensure that expenditures do not exceed appropriations. The final amendment to the budget was adopted in June 2018. A schedule showing the Agency's original and final budget amounts compared with amounts actually paid and received is provided in required supplemental information of these financial statements.

General Fund Budgetary Highlights

The General Fund's actual revenue was \$45.3 million. That amount is above the original budget estimate of \$44.9 million and below the final amended budget of \$48.5 million. The \$3.3 million variance between the final amended budget and the 2018 actual results was due to the deferral of federal, state, and local grants received in the current fiscal year to be spent in the next fiscal year.

The actual expenditures and other financing uses of the General Fund were \$45.1 million and below the final amended budget of \$48.5 million. The \$3.5 million variance between the final amended budget and the 2018 actual results was primarily due to the anticipation of fully expending grant revenue. Expenditures will be incurred in the next fiscal year.

The General Fund had total revenue of \$45.3 million and total expenditures and transfers of \$45.1 million, with an ending fund balance of \$6.9 million.

Special Education Fund Budgetary Highlights

The Special Education Fund's actual revenue was \$54.3 million. That amount is above the original budget estimate of \$50.1 million and above the final amended budget of \$53.6 million.

The actual expenditures and other financing uses of the Special Education Fund were \$54.9 million and are consistent with the final amended budget of \$54.8 million.

Kalamazoo Regional Educational Service Agency

Management's Discussion and Analysis (Continued)

Capital Assets and Debt Administration

Capital Assets

As of June 30, 2018, the Agency had \$27.0 million invested in a broad range of capital assets, including land, buildings, vehicles, furniture, and equipment.

| | Governmental Activities | |
|--|-------------------------|----------------------|
| | 2018 | 2017 |
| Land | \$ 390,377 | \$ 390,377 |
| Construction in progress | 47,770 | 14,587 |
| Buildings and improvements | 34,572,807 | 34,454,119 |
| Furniture and equipment | 6,832,316 | 6,524,727 |
| Total capital assets | 41,843,270 | 41,383,810 |
| Less accumulated depreciation | 14,886,022 | 13,802,301 |
| Total capital assets - Net of accumulated depreciation | \$ 26,957,248 | \$ 27,581,509 |

Debt

At the end of this year, the Agency had \$8.1 million in bonds outstanding versus \$10.4 million in the previous year - a change of approximately 22.1 percent.

The State limits the amount of general obligation debt that schools can issue to 15 percent of the assessed value of all taxable property within the Agency's boundaries. If the Agency issues "qualified debt" (i.e., debt backed by the State of Michigan), such obligations are not subject to this debt limit. The Agency's outstanding unqualified general obligation debt of \$8.1 million is significantly below the State's statutorily imposed limit.

Other obligations include accrued vacation pay, sick leave, and early retirement incentive. We present more detailed information about our long-term liabilities in the notes to the financial statements.

Kalamazoo Regional Educational Service Agency

Statement of Net Position

June 30, 2018

| | Primary Government | | |
|--|----------------------------|-----------------------------|------------------------|
| | Governmental Activities | Business-type Activities | Total |
| Assets | | | |
| Cash and investments (Note 4) | \$ 14,838,666 | \$ 80,381 | \$ 14,919,047 |
| Receivables: | | | |
| Taxes receivable | 219,255 | - | 219,255 |
| Accounts receivable | 1,127,909 | 17,586 | 1,145,495 |
| Due from other governments | 7,895,532 | - | 7,895,532 |
| Internal balances (Note 7) | - | 51,466 | 51,466 |
| Inventories | 108,954 | 4,465 | 113,419 |
| Prepaid assets | 12,720 | - | 12,720 |
| Restricted assets (Note 4) | 259,922 | - | 259,922 |
| Capital assets - Net (Note 6) | 26,957,248 | - | 26,957,248 |
| Total assets | 51,420,206 | 153,898 | 51,574,104 |
| Deferred Outflows of Resources | | | |
| Deferred charges on bond refunding (Note 8) | 144,155 | - | 144,155 |
| Deferred pension costs (Note 10) | 20,963,659 | 350,148 | 21,313,807 |
| Deferred OPEB costs (Note 10) | 1,577,740 | 19,285 | 1,597,025 |
| Total deferred outflows of resources | 22,685,554 | 369,433 | 23,054,987 |
| Liabilities | | | |
| Accounts payable | 1,569,522 | 4,935 | 1,574,457 |
| Due to other governmental units | 2,984,909 | - | 2,984,909 |
| Internal balances (Note 7) | 60,134 | - | 60,134 |
| Accrued payroll and other liabilities | 3,838,797 | 30,289 | 3,869,086 |
| Unearned revenue (Note 5) | 4,018,293 | - | 4,018,293 |
| Noncurrent liabilities: | | | |
| Due within one year (Note 8) | 3,534,501 | - | 3,534,501 |
| Due in more than one year (Note 8) | 6,467,325 | - | 6,467,325 |
| Net pension liability (Note 10) | 77,781,274 | 1,142,298 | 78,923,572 |
| Net OPEB liability (Note 10) | 26,661,209 | 368,045 | 27,029,254 |
| Total liabilities | 126,915,964 | 1,545,567 | 128,461,531 |
| Deferred Inflows of Resources | | | |
| Revenue in support of pension contributions made subsequent to the report date (Note 10) | 3,146,107 | 44,762 | 3,190,869 |
| Deferred pension cost (Note 10) | 4,085,263 | 86,383 | 4,171,646 |
| Deferred OPEB cost (Note 10) | 894,596 | 19,190 | 913,786 |
| Total deferred inflows of resources | 8,125,966 | 150,335 | 8,276,301 |
| Net Position | | | |
| Net investment in capital assets | 19,016,403 | - | 19,016,403 |
| Restricted - Debt Service | 237,091 | - | 237,091 |
| Unrestricted | (80,189,664) | (1,172,571) | (81,362,235) |
| Total net position | \$ (60,936,170) | \$ (1,172,571) | \$ (62,108,741) |

Kalamazoo Regional Educational Service Agency

Statement of Activities

Year Ended June 30, 2018

| Functions/Programs | Expenses | Program Revenue | | Net (Expense) Revenue and Changes in Net Position | | |
|--|-----------------------|----------------------|------------------------------------|---|--------------------------|------------------------|
| | | Charges for Services | Operating Grants and Contributions | Governmental Activities | Business-type Activities | Total |
| Primary government: | | | | | | |
| Governmental activities: | | | | | | |
| Instruction | \$ 23,411,724 | \$ 8,988 | \$ 14,939,490 | \$ (8,463,246) | \$ - | \$ (8,463,246) |
| Support services | 33,852,702 | 6,302,138 | 13,969,741 | (13,580,823) | - | (13,580,823) |
| Community services | 4,266,918 | 276,069 | 4,879,742 | 888,893 | - | 888,893 |
| Intergovernmental transfers | 39,695,222 | - | 7,934,160 | (31,761,062) | - | (31,761,062) |
| Interest | 194,991 | - | - | (194,991) | - | (194,991) |
| Depreciation expense (unallocated) | 1,072,141 | - | - | (1,072,141) | - | (1,072,141) |
| Total governmental activities | 102,493,698 | 6,587,195 | 41,723,133 | (54,183,370) | - | (54,183,370) |
| Business-type activities - Technology | 2,536,533 | 2,313,626 | - | - | (222,907) | (222,907) |
| Total primary government | \$ 105,030,231 | \$ 8,900,821 | \$ 41,723,133 | (54,183,370) | (222,907) | (54,406,277) |
| General revenue: | | | | | | |
| Taxes: | | | | | | |
| Property taxes, levied for general purposes | | | | 12,255,864 | - | 12,255,864 |
| Property taxes, levied for debt service | | | | 2,835,307 | - | 2,835,307 |
| Property taxes, levied for special education | | | | 32,783,822 | - | 32,783,822 |
| State aid not restricted to specific purposes | | | | 5,877,228 | - | 5,877,228 |
| Interest and investment earnings | | | | 122,108 | 184 | 122,292 |
| Other | | | | 284,942 | - | 284,942 |
| Total general revenue | | | | 54,159,271 | 184 | 54,159,455 |
| Transfers | | | | (200,000) | 200,000 | - |
| Change in Net Position | | | | (224,099) | (22,723) | (246,822) |
| Net Position - Beginning of year, as previously reported | | | | (33,762,270) | (767,194) | (34,529,464) |
| Cumulative Effect of Change in Accounting (Note 2) | | | | (26,949,801) | (382,654) | (27,332,455) |
| Net Position - Beginning of year | | | | (60,712,071) | (1,149,848) | (61,861,919) |
| Net Position - End of year | | | | \$ (60,936,170) | \$ (1,172,571) | \$ (62,108,741) |

Kalamazoo Regional Educational Service Agency

Governmental Funds Balance Sheet

June 30, 2018

| | General Fund | Special Education Fund | Nonmajor Funds | Total Governmental Funds |
|---|----------------------|------------------------------|---------------------|--------------------------------|
| Assets | | | | |
| Cash and investments (Note 4) | \$ 9,522,104 | \$ 3,487,659 | \$ 1,828,903 | \$ 14,838,666 |
| Receivables: | | | | |
| Taxes receivable | 56,475 | 150,298 | 12,482 | 219,255 |
| Accounts receivable | 1,047,516 | 80,393 | - | 1,127,909 |
| Due from other governments | 4,284,940 | 3,610,592 | - | 7,895,532 |
| Due from other funds (Note 7) | 794 | 164,703 | 400,569 | 566,066 |
| Inventories | 108,954 | - | - | 108,954 |
| Prepaid assets | 12,720 | - | - | 12,720 |
| Restricted assets (Note 4) | - | - | 259,922 | 259,922 |
| | <u>\$ 15,033,503</u> | <u>\$ 7,493,645</u> | <u>\$ 2,501,876</u> | <u>\$ 25,029,024</u> |
| Total assets | | | | |
| Liabilities | | | | |
| Accounts payable | \$ 1,270,512 | \$ 261,602 | \$ 37,408 | \$ 1,569,522 |
| Due to other governmental units | 174,103 | 2,810,806 | - | 2,984,909 |
| Due to other funds (Note 7) | 1,112,996 | 780,561 | - | 1,893,557 |
| Accrued payroll and other liabilities | 1,697,444 | 2,117,367 | - | 3,814,811 |
| Unearned revenue (Note 5) | 3,848,375 | 169,918 | - | 4,018,293 |
| | <u>8,103,430</u> | <u>6,140,254</u> | <u>37,408</u> | <u>14,281,092</u> |
| Total liabilities | | | | |
| Deferred Inflows of Resources - Unavailable revenue (Note 5) | | | | |
| | <u>53,267</u> | <u>141,929</u> | <u>11,774</u> | <u>206,970</u> |
| Total liabilities and deferred inflows of resources | 8,156,697 | 6,282,183 | 49,182 | 14,488,062 |
| Fund Balances | | | | |
| Nonspendable: | | | | |
| Inventory | 108,954 | - | - | 108,954 |
| Prepaid assets | 12,720 | - | - | 12,720 |
| Restricted: | | | | |
| Debt service | - | - | 261,077 | 261,077 |
| Special education | - | 1,211,462 | - | 1,211,462 |
| Committed - Building and site improvements | - | - | 2,191,617 | 2,191,617 |
| Assigned: | | | | |
| Budgeted use of fund balance for 2018- 2019 | 219,262 | - | - | 219,262 |
| Regional transportation and safety institute | 347,555 | - | - | 347,555 |
| Unassigned | 6,188,315 | - | - | 6,188,315 |
| | <u>6,876,806</u> | <u>1,211,462</u> | <u>2,452,694</u> | <u>10,540,962</u> |
| Total fund balances | | | | |
| Total liabilities, deferred inflows of resources, and fund balances | <u>\$ 15,033,503</u> | <u>\$ 7,493,645</u> | <u>\$ 2,501,876</u> | <u>\$ 25,029,024</u> |

Kalamazoo Regional Educational Service Agency

Governmental Funds

Reconciliation of the Balance Sheet to the Statement of Net Position

June 30, 2018

| | |
|---|--------------------------------------|
| Fund Balances Reported in Governmental Funds | \$ 10,540,962 |
| Amounts reported for governmental activities in the statement of net position are different because: | |
| Capital assets used in governmental activities are not financial resources and are not reported in the funds: | |
| Cost of capital assets | 41,843,270 |
| Accumulated depreciation | <u>(14,886,022)</u> |
| Net capital assets used in governmental activities | 26,957,248 |
| Receivables that are not collected soon after year end are not available to pay for current period expenditures and, therefore, are reported as unavailable revenue in the funds. | 206,970 |
| Deferred inflows and outflows related to bond refundings are not reported in the funds | 144,155 |
| Bonds payable, including premiums, are not due and payable in the current period and are not reported in the funds | (8,085,000) |
| Accrued interest is not due and payable in the current period and is not reported in the funds | (23,986) |
| Some employee fringe benefits are payable over a long period of years and do not represent a claim on current financial resources; therefore, they are not reported as fund liabilities: | |
| Employee compensated absences | (649,470) |
| Early termination incentive obligations | (1,267,356) |
| Net pension liability and related deferred inflows and outflows | (60,902,878) |
| Net OPEB liability and related deferred inflows and outflows | (25,978,065) |
| Revenue in support of pension contributions made subsequent to the measurement date is reported as a deferred inflow of resources in the statement of net position and is not reported in the funds | (3,146,107) |
| Internal service funds are included as part of governmental activities | <u>1,267,357</u> |
| Net Position of Governmental Activities | <u><u>\$ (60,936,170)</u></u> |

Kalamazoo Regional Educational Service Agency

Governmental Funds

Statement of Revenue, Expenditures, and Changes in Fund Balances

Year Ended June 30, 2018

| | General Fund | Special Education Fund | Nonmajor Funds | Total Governmental Funds |
|--|---------------------|------------------------------|---------------------|--------------------------------|
| Revenue | | | | |
| Local sources | \$ 15,923,746 | \$ 34,994,062 | \$ 2,946,771 | \$ 53,864,579 |
| State sources | 13,643,980 | 10,841,762 | 114,553 | 24,600,295 |
| Federal sources | 9,679,311 | 8,444,600 | - | 18,123,911 |
| Interdistrict sources | 6,023,302 | - | - | 6,023,302 |
| Total revenue | 45,270,339 | 54,280,424 | 3,061,324 | 102,612,087 |
| Expenditures | | | | |
| Current: | | | | |
| Instruction | 4,699,235 | 17,771,573 | - | 22,470,808 |
| Support services | 17,560,097 | 14,677,912 | - | 32,238,009 |
| Community services | 4,110,427 | - | - | 4,110,427 |
| Debt service: | | | | |
| Principal | - | - | 2,500,000 | 2,500,000 |
| Interest | - | - | 373,384 | 373,384 |
| Other | - | - | 60,105 | 60,105 |
| Capital outlay | 583,728 | 241,619 | 215,615 | 1,040,962 |
| Intergovernmental transfers | 17,697,262 | 21,997,960 | - | 39,695,222 |
| Total expenditures | 44,650,749 | 54,689,064 | 3,149,104 | 102,488,917 |
| Excess of Revenue Over (Under) Expenditures | 619,590 | (408,640) | (87,780) | 123,170 |
| Other Financing Sources (Uses) | | | | |
| Face value of debt issued | - | - | 8,235,000 | 8,235,000 |
| Transfers in | - | - | 400,000 | 400,000 |
| Payment to bond refunding escrow agent | - | - | (8,177,635) | (8,177,635) |
| Transfers out | (400,000) | (200,000) | - | (600,000) |
| Total other financing (uses) sources | (400,000) | (200,000) | 457,365 | (142,635) |
| Net Change in Fund Balances | 219,590 | (608,640) | 369,585 | (19,465) |
| Fund Balances - Beginning of year | 6,657,216 | 1,820,102 | 2,083,109 | 10,560,427 |
| Fund Balances - End of year | \$ 6,876,806 | \$ 1,211,462 | \$ 2,452,694 | \$ 10,540,962 |

Kalamazoo Regional Educational Service Agency

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

Year Ended June 30, 2018

| | |
|---|----------------------------|
| Net Change in Fund Balance Reported in Governmental Funds | \$ (19,465) |
| Amounts reported for governmental activities in the statement of activities are different because: | |
| Governmental funds report capital outlays as expenditures; however, in the statement of activities, these costs are allocated over their estimated useful lives as depreciation: | |
| Capitalized capital outlay | 447,880 |
| Depreciation expense | (1,072,141) |
| Revenue in the statement of activities that does not provide current financial resources is not reported as revenue in the funds until it is available | (118,528) |
| Revenue in support of pension contributions made subsequent to the measurement date | (873,087) |
| Issuing debt, net of premiums and discounts, provides current financial resources to governmental funds, but increases long-term liabilities in the statement of net position | (8,235,000) |
| Repayment of bond principal is an expenditure in the governmental funds, but not in the statement of activities (where it reduces long-term debt); amortization of premium/discounts and inflows/outflows related to bond refundings are not expenses in the governmental funds | 10,866,629 |
| Interest expense is recognized in the government-wide statements as it accrues | 49,504 |
| Some employee costs (pension, OPEB, compensated absences, early retirement incentives) do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental funds | (1,269,891) |
| Change in Net Position of Governmental Activities | <u>\$ (224,099)</u> |

Kalamazoo Regional Educational Service Agency

Proprietary Funds Statement of Net Position

June 30, 2018

| | Enterprise Fund | Governmental Activities |
|--|-----------------------|----------------------------|
| | Technology Fund | Internal Service Fund |
| Assets | | |
| Current assets: | | |
| Cash (Note 4) | \$ 80,381 | \$ - |
| Receivables - Other receivables | 17,586 | - |
| Due from other funds (Note 7) | 121,804 | 1,267,357 |
| Inventories | 4,465 | - |
| Total assets | 224,236 | 1,267,357 |
| Deferred Outflows of Resources | | |
| Deferred pension costs (Note 10) | 350,148 | - |
| Deferred OPEB costs (Note 10) | 19,285 | - |
| Total deferred outflows of resources | 369,433 | - |
| Liabilities | | |
| Current liabilities: | | |
| Accounts payable | 4,935 | - |
| Due to other funds (Note 7) | 70,338 | - |
| Accrued payroll and other liabilities | 30,289 | - |
| Total current liabilities | 105,562 | - |
| Noncurrent liabilities: | | |
| Net pension liability (Note 10) | 1,142,298 | - |
| Net OPEB liability (Note 10) | 368,045 | - |
| Total noncurrent liabilities | 1,510,343 | - |
| Total liabilities | 1,615,905 | - |
| Deferred Inflows of Resources (Note 10) | | |
| Revenue in support of pension contributions made subsequent to the report date | 44,762 | - |
| Deferred pension cost | 86,383 | - |
| Deferred OPEB cost | 19,190 | - |
| Total deferred inflows of resources | 150,335 | - |
| Net Position - Unrestricted | \$ (1,172,571) | \$ 1,267,357 |

Kalamazoo Regional Educational Service Agency

Proprietary Funds
Statement of Revenue, Expenses, and Changes in Net Position

Year Ended June 30, 2018

| | Enterprise Fund | Governmental Activities |
|---|--------------------|----------------------------|
| | Technology Fund | Internal Service Fund |
| Operating Revenue | | |
| Charges to other funds | \$ - | \$ 409,216 |
| Charges to other districts | 2,313,626 | - |
| Total operating revenue | 2,313,626 | 409,216 |
| Operating Expenses | | |
| Technology support expenses | 2,536,533 | - |
| Retirement program benefits | - | 314,056 |
| Total operating expenses | 2,536,533 | 314,056 |
| Operating (Loss) Income | (222,907) | 95,160 |
| Nonoperating Revenue - Interest and investment earnings | 184 | - |
| Transfers In (Note 7) | 200,000 | - |
| Change in Net Position | (22,723) | 95,160 |
| Net Position - Beginning of year, as previously reported | (767,194) | 1,172,197 |
| Cumulative Effect of Change in Accounting (Note 2) | (382,654) | - |
| Net Position - Beginning of year | (1,149,848) | 1,172,197 |
| Net Position - End of year | \$ (1,172,571) | \$ 1,267,357 |

Kalamazoo Regional Educational Service Agency

Proprietary Funds Statement of Cash Flows

Year Ended June 30, 2018

| | Enterprise Fund | Governmental Activities |
|--|--------------------|----------------------------|
| | Technology Fund | Internal Service Fund |
| Cash Flows from Operating Activities | | |
| Payments to other funds | \$ (101,865) | \$ - |
| Payments for supplies and purchased services | (1,597,749) | - |
| Payments for employee compensation | (891,325) | - |
| Receipts from other governments | 2,504,221 | - |
| Net cash used in operating activities | (86,718) | - |
| Cash Flows Provided by Investing Activities - Interest | 184 | - |
| Net Decrease in Cash | (86,534) | - |
| Cash - Beginning of year | 166,915 | - |
| Cash - End of year | \$ 80,381 | \$ - |
| Reconciliation of Operating (Loss) Income to Net Cash from Operating Activities | | |
| Operating (loss) income | \$ (222,907) | 95,160 |
| Adjustments to reconcile operating (loss) income to net cash from operating activities - | | |
| Changes in assets and liabilities: | | |
| Receivables | (9,919) | - |
| Due to and from other funds | (101,865) | (95,160) |
| Inventories and prepaid assets | (802) | - |
| Accounts payable and accrued liabilities | 160,040 | - |
| Net pension liability | 119,828 | - |
| Net OPEB Liability | (31,093) | - |
| Net cash used in operating activities | \$ (86,718) | \$ - |

Kalamazoo Regional Educational Service Agency

Fiduciary Funds Statement of Fiduciary Assets and Liabilities

June 30, 2018

| | Student Activities Agency Fund |
|-------------------------------|--------------------------------------|
| Assets | |
| Cash and investments (Note 4) | \$ 178,839 |
| Receivables | 5,011 |
| Due from other funds (Note 7) | <u>8,668</u> |
| Total assets | <u>\$ 192,518</u> |
| Liabilities | |
| Accounts payable | \$ 2,587 |
| Due to student groups | <u>189,931</u> |
| Total liabilities | <u>\$ 192,518</u> |

June 30, 2018

Note 1 - Nature of Business

Kalamazoo Regional Educational Service Agency (the "Agency") is a regional educational service agency in the state of Michigan that provides educational services to students.

Note 2 - Significant Accounting Policies

Accounting and Reporting Principles

The Agency follows accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. Accounting and financial reporting pronouncements are promulgated by the Governmental Accounting Standards Board. The following is a summary of the significant accounting policies used by the Agency:

Reporting Entity

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

Report Presentation

Governmental accounting principles require that financial reports include two different perspectives - the Agency-wide perspective and the fund-based perspective. The Agency-wide financial statements (i.e., the statement of net position and the statement of activities) report information on all of the nonfiduciary activities of the primary government. The Agency-wide financial statements are presented on the economic resources measurement focus and the full accrual basis of accounting. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. The statements also present a schedule reconciling these amounts to the modified accrual-based presentation found in the fund-based statements.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenue. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenue includes: (1) charges to customers or applicants for goods, services, or privileges provided; (2) operating grants and contributions; and (3) capital grants and contributions, including special assessments. Taxes, unrestricted intergovernmental receipts, and other items not properly included among program revenue are reported instead as general revenue.

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

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the Agency-wide financial statements. Major individual governmental funds and major individual enterprise funds, if any, are reported as separate columns in the fund financial statements.

June 30, 2018

Note 2 - Significant Accounting Policies (Continued)

Fund Accounting

The Agency accounts for its various activities in several different funds in order to demonstrate accountability for how it spends certain resources; separate funds allow the Agency to show the particular expenditures for which specific revenue is used. The various funds are aggregated into three broad fund types:

Governmental Funds

Governmental funds include all activities that provide general governmental services that are not business-type activities. Governmental funds can include the General Fund, special revenue funds, debt service funds, capital project funds, and permanent funds. The Agency reports the following funds as “major” governmental funds:

- The General Fund is the primary operating fund because it accounts for all financial resources of the Agency other than those specifically assigned to another fund.
- The Special Education Fund is a special revenue fund used to account for resources that provide special education programs for the Agency. These programs are funded primarily by taxes, state aid categoricals, Medicaid funding, and federal grants. Any operating deficit generated by these activities is the responsibility of the General Fund.

Additionally, the Agency reports the following nonmajor governmental fund types:

- The capital project funds are used to account for nonbond-funded resources specifically designed for the acquisition and construction of facilities and for major capital improvements. The Agency has the General Education Capital Projects Fund and the Special Education Capital Projects Fund for related improvements.
- The Debt Service Fund is used to record property tax, interest, and state aid revenue and the payment of principal and interest on long-term debt related to the 2017 Refunding Bonds.

Proprietary Funds

Proprietary funds include enterprise funds (which provide goods or services to users in exchange for charges or fees) and internal service funds (which provide goods or services to other funds of the Agency). The Agency reports the following fund as a “major” enterprise fund:

- The Technology Fund is an enterprise fund used to account for the operations of the Agency's Technology Services Consortium.

Additionally, the Agency reports the following nonmajor proprietary fund type:

- The Internal Service Fund accounts for retirement incentives provided to retirees of the Agency.

Fiduciary Funds

Fiduciary funds include amounts held in a fiduciary capacity for others. These amounts are not used to operate the Agency's programs. The Agency maintains a student activity agency fund to record the transactions of student groups for school and school-related purposes. The fund is segregated and held in trust for the students.

Specific Balances and Transactions

Cash and Investments

Cash and investments include cash on hand, demand deposits, and short-term investments with a maturity of three months or less when acquired. Investments are stated at amortized cost.

Note 2 - Significant Accounting Policies (Continued)

Receivables

In general, outstanding balances between funds are reported as “due to/from other funds.” Activities between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as “advances to/from other funds.” Any residual balances outstanding between the governmental activities and the business-type activities are reported in the Agency-wide financial statements as “internal balances.” The Agency considers all receivables to be fully collectible; accordingly, no allowance for uncollectible amounts is recorded.

Inventories and Prepaid Items

Inventories are valued at cost, on a first-in, first-out basis. Certain payments to vendors reflect costs applicable to future fiscal years and are recorded as prepaid items in both Agency-wide and fund financial statements.

Restricted Assets

The unspent property tax revenue and related interest of the Debt Service Fund require amounts to be set aside for future bond payments. These amounts have been classified as restricted assets.

Capital Assets

Capital assets, which include land, buildings, equipment, and vehicles, are reported in the applicable governmental activities column in the Agency-wide financial statements. Capital assets are defined by the Agency as assets with an initial individual cost of more than \$5,000 and an estimated useful life in excess of one year. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated acquisition value at the date of donation.

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

| | <u>Depreciable Life - Years</u> |
|----------------------------|-------------------------------------|
| Buildings and improvements | 20 to 50 |
| Furniture and equipment | 5 to 20 |
| Vehicles | 5 to 20 |

Long-term Obligations

In the Agency-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the statement of net position. Bond premiums and discounts are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are expensed at the time they are incurred. In the fund financial statements, governmental fund types recognize bond issuances and premiums as an “other financing source” and bond discounts as “other financing uses.” The General Fund and Debt Service Fund are generally used to liquidate governmental long-term debt.

Deferred Outflows/Inflows of Resources

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element represents a consumption of net position that applies to future periods and will not be recognized as an outflow of resources (expense/expenditure) until then.

The Agency reports deferred outflows related to deferred charges on refundings and deferred pension and OPEB costs.

Note 2 - Significant Accounting Policies (Continued)

In addition to liabilities, the statement of net position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element represents an acquisition of net position that applies to future periods and will not be recognized as an inflow of resources (revenue) until that time.

The Agency reports deferred inflows related to revenue in support of pension contributions made subsequent to the measurement date and deferred pension and OPEB cost reductions.

Fund Balance Policies

Fund balance of governmental funds is reported in various categories based on the nature of any limitations requiring the use of resources for specific purposes. The Agency itself can establish limitations on the use of resources through either a commitment (committed fund balance) or an assignment (assigned fund balance).

The committed fund balance classification includes amounts that can be used only for the specific purposes determined by a formal action of the Agency's highest level of decision-making authority. The Board of Education is the highest level of decision-making authority for the Agency that can, by adoption of an ordinance prior to the end of the fiscal year, commit fund balance. Once adopted, the limitation imposed by the ordinance remains in place until a similar action is taken (the adoption of another ordinance) to remove or revise the limitation.

Amounts in the assigned fund balance classification are intended to be used by the government for specific purposes, but do not meet the criteria to be classified as committed. The Agency has, by resolution, authorized the assistant superintendent to assign fund balance. The Board of Education may also assign fund balance as it does when appropriating fund balance to cover a gap between estimated revenue and appropriations in the subsequent year's appropriated budget. Unlike commitments, assignments generally only exist temporarily. In other words, an additional action does not normally have to be taken for the removal of an assignment. Conversely, as discussed above, an additional action is essential to either remove or revise a commitment.

Property Tax Revenue

Property taxes are levied on July 1 and December 1 by the 27 municipalities within the Agency's boundaries. Property tax revenue is recognized when levied to the extent it is deemed to be collectible. The municipalities bill and collect property taxes until March 15, at which time real property taxes are turned over to the counties for reimbursement from their revolving tax funds. The municipalities continue to collect delinquent personal property taxes. The Agency considers all receivables to be fully collectible; accordingly, no allowance for uncollectible amounts is recorded.

Pension and Other Postemployment Benefit (OPEB) Plans

For purposes of measuring the net pension and net OPEB liabilities, deferred outflows of resources and deferred inflows of resources related to each plan, and pension and OPEB expense, information about the fiduciary net position of the Michigan Public School Employees' Retirement System (MPERS) and additions to/deductions from MPERS fiduciary net position have been determined on the same basis as they are reported by MPERS. MPERS uses the economic resources measurement focus and the full accrual basis of accounting. Contribution revenue is recorded as contributions are due, pursuant to legal requirements. Benefit payments (including refunds of employee contributions) are recognized as expenses when due and payable in accordance with the plan benefit terms. Related plan investments are reported at fair value.

Note 2 - Significant Accounting Policies (Continued)

Compensated Absences and Early Retirement Incentive

It is the Agency's policy to permit employees to accumulate earned but unused sick and vacation pay benefits. Sick pay is accrued for the estimated amount that the Agency will pay upon employment termination; vacation pay is accrued when incurred. Both of these are reported in the government-wide and proprietary fund financial statements. A liability for these amounts is reported in governmental funds only for employee terminations as of year end. Generally, the funds that report each employee's compensation are used to liquidate the obligations.

A liability for retirement incentives reported in the Agency-wide statements consists of payments due to individuals who were eligible and elected to accept the incentive offer. A liability for these amounts is reported in governmental funds as it comes due for payment. The compensated absences liability has been calculated using the vesting method, in which leave amounts for both employees who are currently eligible to receive termination payments at the normal retirement age and other employees who are expected to become eligible in the future to receive such payments upon normal retirement are included.

Use of Estimates

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

Adoption of New Accounting Pronouncements

As of July 1, 2017, the Agency adopted GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pensions*, which addresses reporting by governments that provide postemployment benefits other than pensions (OPEB) to their employees and for governments that finance OPEB for employees of other governments. This OPEB standard will require the Agency to recognize on the face of the financial statements its proportionate share of the net OPEB liability related to its participation in the Michigan Public School Employees' Retirement System (MPSERS). The statement also enhances accountability and transparency through revised note disclosures and required supplemental information (RSI).

In accordance with the statement, the Agency has reported a net OPEB liability of \$28,509,875, deferred outflows of financial resources for OPEB contributions of \$2,036,146 made subsequent to the measurement date, and deferred inflows of financial resources for revenue received from State Aid in support of OPEB contributions of \$858,726 that was received subsequent to the measurement date, as the effects of these changes in accounting principles on the Agency's net position as of July 1, 2017.

Upcoming Accounting Pronouncements

In January 2017, the Governmental Accounting Standards Board issued Statement No. 84, *Fiduciary Activities*. This statement establishes criteria for identifying fiduciary activities of all state and local governments. An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements. The Agency is currently evaluating the impact this standard will have on the financial statements when adopted. The provisions of this statement are effective for the Agency's financial statements for the year ending June 30, 2020.

Note 2 - Significant Accounting Policies (Continued)

In June 2017, the Governmental Accounting Standards Board issued GASB Statement No. 87, *Leases*, which improves accounting and financial reporting for leases by governments. This statement requires recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources. The Agency is currently evaluating the impact this standard will have on the financial statements when adopted. The provisions of this statement are effective for the Agency's financial statements for the year ending June 30, 2021.

In March 2018, the GASB issued Statement No. 88, *Certain Disclosures Related to Debt, Including Direct Borrowings and Direct Placements*. This statement establishes criteria to improve the information that is disclosed in the notes to the government financial statements related to debt, including direct borrowings and direct placements. It also clarifies which liabilities governments should include when disclosing information related to debt. The Agency is currently evaluating the impact this standard will have on the financial statements when adopted. The provisions of this statement are effective for the Agency's financial statements for the year ending June 30, 2019.

Note 3 - Stewardship, Compliance, and Accountability

Budgetary Information

Annual budgets are adopted on a basis consistent with generally accepted accounting principles and state law for the General Fund and all special revenue funds. All annual appropriations lapse at fiscal year end. The budget document presents information by fund and function. The legal level of budgetary control adopted by the governing body (i.e., the level at which expenditures may not legally exceed appropriations) is the function level. State law requires the Agency to have its budget in place by July 1. Expenditures in excess of amounts budgeted are a violation of Michigan law. State law permits districts to amend their budgets during the year. During the year, the budget was amended in a legally permissible manner. The School District changed budgeted amounts during the year in response to revised revenue estimates.

Encumbrance accounting is employed in governmental funds. Encumbrances (e.g., purchase orders, contracts) are not tracked during the year. Budget appropriations are considered to be spent once the goods are delivered or the services rendered.

Excess of Expenditures Over Appropriations in Budgeted Funds

The Agency did not have significant expenditure budget variances.

Fund Deficits

Under Michigan law, agencies are required to maintain positive fund balance in each fund. The Agency has an accumulated net position deficit in the Technology Fund. This deficit is due to the inclusion of the Technology Fund's proportionate share of the net pension liability and will be eliminated through future required contributions to the Michigan Public School Employees' Retirement System.

Note 4 - Deposits and Investments

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

The Agency has designated two financial institutions for the deposit of its funds.

The Agency's cash and investments are subject to several types of risk, which are examined in more detail below:

Custodial Credit Risk of Bank Deposits

Custodial credit risk is the risk that in the event of a bank failure, the Agency's deposits may not be returned to it. The Agency has a deposit policy for custodial credit risk. At year end, the Agency had \$7,219,565 of bank deposits (certificates of deposit and checking and savings accounts) that were uninsured and uncollateralized. The Agency believes that due to the dollar amounts of cash deposits and the limits of FDIC insurance, it is impractical to insure all deposits. As a result, the Agency evaluates each financial institution with which it deposits funds and assesses the level of risk of each institution; only those institutions with an acceptable estimated risk level are used as depositories.

Custodial Credit Risk of Investments

Custodial credit risk is the risk that, in the event of the failure of the counterparty, the Agency will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The Agency's policy for custodial credit risk states custodial credit risk will be minimized by limiting investments to the types of securities allowed by state law, as described in the policy, and by prequalifying the financial institutions, broker/dealers, intermediaries, and advisors with which the Agency will do business using the criteria established in the investment policy. At June 30, 2018, the Agency does not have investments with custodial credit risk.

Interest Rate Risk

Interest rate risk is the risk that the value of investments will decrease as a result of a rise in interest rates. The Agency's investment policy does not restrict investment maturities other than commercial paper, which can only be purchased with a 270-day maturity. The Agency's policy minimizes interest rate risk by structuring the investment portfolio so that securities mature to meet cash requirements for ongoing operations, thereby avoiding the need to sell securities in the open market; investing operating funds primarily in shorter-term securities, liquid asset funds, money market mutual funds, or similar investment pools; and limiting the average maturity in accordance with the Agency's cash requirements.

Credit Risk

State law limits investments in commercial paper to the top two ratings issued by nationally recognized statistical rating organizations. The Agency has no investment policy that would further limit its investment choices. As of year end, the credit quality ratings of debt securities (other than the U.S. government) are as follows:

| Investment | Amortized Cost | Rating | Rating Organization |
|--|----------------|--------|---------------------|
| Michigan Liquid Asset Fund - MAX Class | \$ 8,175,656 | AAAm | S&P |

Note 4 - Deposits and Investments (Continued)

Investment Restrictions

The Michigan Liquid Asset Fund - MAX Class investment that may not be redeemed for at least 14 calendar days with the exception of direct investments of funds distributed by the State of Michigan. In addition, redemptions made prior to the 14-day period are subject to a penalty equal to 15 days' interest on the amount so redeemed.

Concentration of Credit Risk

The Agency's investment policy minimizes concentration of credit risk by requiring diversification of the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimized. The Agency does not have any investments subject to concentration of credit risk.

Foreign Currency Risk

Foreign currency risk is the risk that an investment denominated in the currency of a foreign country could reduce its U.S. dollar value as a result of changes in foreign currency exchange rates. State law and the Agency's investment policy prohibit investments in foreign currency.

Note 5 - Unavailable/Unearned Revenue

Governmental funds report unavailable revenue in connection with receivables for revenue that is not considered to be available to liquidate liabilities of the current period. Governmental funds also report unearned revenue recognition in connection with resources that have been received but not yet earned.

At June 30, 2018, the various components of unearned and unavailable revenue were as follows:

| | Governmental Funds | |
|--|----------------------------------|-------------------------|
| | Deferred Inflow - Unavailable | Liability - Unearned |
| Delinquent property taxes | \$ 206,970 | \$ - |
| Grant and categorical aid payment received prior to meeting all eligibility requirements | - | 4,018,293 |
| Total | <u>\$ 206,970</u> | <u>\$ 4,018,293</u> |

Kalamazoo Regional Educational Service Agency

Notes to Financial Statements

June 30, 2018

Note 6 - Capital Assets

Capital asset activity of the Agency's governmental and business-type activities was as follows:

Governmental Activities

| | Balance July 1, 2017 | Transfers | Additions | Disposals and Adjustments | Balance June 30, 2018 |
|--|-------------------------|-----------|--------------|------------------------------|--------------------------|
| Capital assets not being depreciated: | | | | | |
| Land | \$ 390,377 | \$ - | \$ - | \$ - | \$ 390,377 |
| Construction in progress | 14,587 | (14,587) | 47,770 | - | 47,770 |
| Subtotal | 404,964 | (14,587) | 47,770 | - | 438,147 |
| Capital assets being depreciated: | | | | | |
| Buildings and improvements | 34,454,119 | 14,587 | 104,101 | - | 34,572,807 |
| Vehicles, furniture, and equipment | 6,524,727 | - | 296,009 | - | 6,820,736 |
| Subtotal | 40,978,846 | 14,587 | 400,110 | - | 41,393,543 |
| Accumulated depreciation: | | | | | |
| Buildings and improvements | 8,107,090 | - | 736,907 | - | 8,843,997 |
| Vehicles, furniture, and equipment | 5,695,211 | - | 335,234 | - | 6,030,445 |
| Subtotal | 13,802,301 | - | 1,072,141 | - | 14,874,442 |
| Net capital assets being depreciated | 27,176,545 | 14,587 | (672,031) | - | 26,519,101 |
| Net governmental activities capital assets | \$ 27,581,509 | \$ - | \$ (624,261) | \$ - | \$ 26,957,248 |

Business-type Activities

| | Balance July 1, 2017 | Additions | Disposals and Adjustments | Balance June 30, 2018 |
|--|-------------------------|-----------|------------------------------|--------------------------|
| Capital assets being depreciated - Furniture and equipment | \$ 11,580 | \$ - | \$ - | \$ 11,580 |
| Accumulated depreciation - Furniture and equipment | 11,580 | - | - | 11,580 |
| Net business-type activities capital assets | \$ - | \$ - | \$ - | \$ - |

Depreciation expense was not charged to activities, as the Agency considers its assets to benefit multiple activities and allocation is not practical.

Construction Commitments

The Agency had no construction commitments at year end.

Note 7 - Interfund Receivables, Payables, and Transfers

The composition of interfund balances is as follows:

| Fund Due To | Fund Due From | | | |
|-------------------------------------|---------------------|------------------------|------------------------------|---------------------|
| | General Fund | Special Education Fund | Enterprise Fund - Technology | Total |
| General Fund | \$ - | \$ 75 | \$ 719 | \$ 794 |
| Special Education Fund | 164,703 | - | - | 164,703 |
| Internal Service Fund | 417,822 | 779,916 | 69,619 | 1,267,357 |
| Enterprise Fund - Technology | 121,234 | 570 | - | 121,804 |
| Fiduciary Fund - Student Activities | 8,668 | - | - | 8,668 |
| Nonmajor governmental funds | 400,569 | - | - | 400,569 |
| Total | \$ 1,112,996 | \$ 780,561 | \$ 70,338 | \$ 1,963,895 |

Interfund balances represent routine and temporary cash flow assistance until amounts are transferred from fund investment accounts.

Interfund transfers reported in the fund financial statements are composed of the following:

| Paying Fund (Transfer Out) | Receiving Fund (Transfer In) | Amount |
|----------------------------|---|-------------------|
| General Fund | General Education Capital Projects Fund | \$ 200,000 |
| | Technology Fund | 200,000 |
| | Total General Fund | 400,000 |
| Special Education Fund | Special Education Capital Projects Fund | 200,000 |
| | Total | \$ 600,000 |

Transfers from the General Fund to the General Education Capital Projects Fund and transfers from the Special Education Fund to the Special Education Capital Projects Fund are to provide funding for future capital projects. Transfers from the General Fund to the Technology Fund are to provide funding for general operating.

Note 8 - Long-term Debt

Long-term debt activity for the year ended June 30, 2018 can be summarized as follows:

| | Beginning Balance | Additions | Reductions | Ending Balance | Due Within One Year |
|---|----------------------|---------------------|------------------------|----------------------|---------------------|
| Bonds payable: | | | | | |
| Bonds | \$ 10,375,000 | \$ 8,235,000 | \$ (10,525,000) | \$ 8,085,000 | \$ 2,710,000 |
| Issuance premiums | 197,474 | - | (197,474) | - | - |
| Total bonds payable | 10,572,474 | 8,235,000 | (10,722,474) | 8,085,000 | 2,710,000 |
| Compensated absences | 599,388 | 333,888 | (283,806) | 649,470 | 649,470 |
| Early termination obligation | 1,172,196 | 409,216 | (314,056) | 1,267,356 | 175,031 |
| Total governmental activities long-term debt | \$ 12,344,058 | \$ 8,978,104 | \$ (11,320,336) | \$ 10,001,826 | \$ 3,534,501 |

At June 30, 2018, the Agency has \$144,155 of deferred charges related to the 2017 bond refunding outstanding.

Note 8 - Long-term Debt (Continued)

General Obligation Bonds

The Agency issues general obligation bonds to provide for the acquisition and construction of major capital facilities and the acquisition of certain equipment. General obligations have been issued for governmental activities. General obligation bonds are direct obligations and pledge the full faith and credit of the Agency. General obligations outstanding at June 30, 2018 are as follows:

| Purpose | Remaining Annual Installments | Interest Rate | Maturing | Outstanding |
|----------------------------------|-------------------------------|---------------|-------------|--------------|
| \$8,235,000 2017 Refunding Bonds | 3 | 1.78 | May 1, 2021 | \$ 8,085,000 |

Other Long-term Liabilities

The liability for compensated absences reported in the Agency-wide financial statements consists of earned, but unused accumulated vacation and sick leave benefits. A liability for retirement incentives reported in the Agency-wide statements consists of payments due to individuals who were eligible and elected to accept the incentive offer. A liability for these amounts is reported in governmental funds as it comes due for payment. The compensated absences liability has been calculated using the vesting method, in which leave amounts for both employees who are currently eligible to receive termination payments at the normal retirement age and other employees who are expected to become eligible in the future to receive such payments upon normal retirement are included.

Debt Service Requirements to Maturity

Annual debt service requirements to maturity for the above bonds and note obligations are as follows:

| Years Ending June 30 | Governmental Activities | | |
|----------------------|-------------------------|------------|--------------|
| | Principal | Interest | Total |
| 2019 | \$ 2,710,000 | \$ 138,350 | \$ 2,848,350 |
| 2020 | 2,785,000 | 89,890 | 2,874,890 |
| 2021 | 2,590,000 | 40,762 | 2,630,762 |
| Total | \$ 8,085,000 | \$ 269,002 | \$ 8,354,002 |

Bond Refunding

During the year, the Agency issued \$8,235,000 in general obligation bonds with an interest rate of 1.78 percent. The proceeds of these bonds were used to advance refund \$8,025,000 of outstanding 2008 bonds with an average interest rate of 5.00 percent. The net proceeds were \$8,177,635 (after payment of \$57,365 in underwriting fees, insurance, and other issuance costs). Those securities were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the original bonds. As a result, the bonds are considered to be defeased, and the liability for the bonds has been removed from the general long-term obligation. The advance refunding reduced total debt service payments over the next three years by approximately \$464,000, which represents an economic gain of approximately \$429,000.

Note 9 - Risk Management

The Agency is exposed to various risks of loss related to property loss, torts, errors and omissions, and employee injuries (workers' compensation), as well as medical benefits provided to employees. The Agency has purchased commercial insurance for property loss, torts, and errors and omissions claims, health, vision, and dental claims. The Agency participates in the SET-SEG risk pool for claims relating to workers' compensation. Settled claims relating to the commercial insurance have not exceeded the amount of insurance coverage in any of the past three fiscal years.

Note 9 - Risk Management (Continued)

The shared-risk pool program in which the Agency participates operates as a common risk-sharing management program for school districts in Michigan; member premiums are used to purchase commercial excess insurance coverage and to pay member claims in excess of deductible amounts.

Note 10 - Michigan Public School Employees' Retirement System

Plan Description

The Agency participates in the Michigan Public School Employees' Retirement System (MPSERS or the "System"), a statewide, cost-sharing, multiple-employer defined benefit public employee retirement system governed by the State of Michigan that covers substantially all employees of the Agency. Certain agency employees also receive defined contribution retirement and healthcare benefits through the System. The System provides retirement, survivor, and disability benefits to plan members and their beneficiaries. The System also provides postemployment healthcare benefits to retirees and beneficiaries who elect to receive those benefits.

The System is administered by the Office of Retirement Services (ORS). The Michigan Public School Employees' Retirement System issues a publicly available financial report that includes financial statements and required supplemental information for the pension and postemployment healthcare plans. That report is available on the web at <http://www.michigan.gov/orsschools>, or by writing to the Office of Retirement System (ORS) at 7150 Harris Drive, P.O. Box 30171, Lansing, MI 48909.

Benefits Provided

Benefit provisions of the defined benefit (DB) pension plan and the postemployment healthcare plan are established by state statute, which may be amended. Public Act 300 of 1980, as amended, establishes eligibility and benefit provisions for the defined benefit pension plan and the postemployment healthcare plan.

Depending on the plan option selected, member retirement benefits are calculated as final average compensation times years of services times a pension factor ranging from 1.25 percent to 1.50 percent. The requirements to retire range from attaining the age of 46 to 60 with years of service ranging from 5 to 30 years, depending on when the employee became a member. Early retirement is computed in the same manner as a regular pension, but is permanently reduced 0.50 percent for each full and partial month between the pension effective date and the date the member will attain age 60. There is no mandatory retirement age.

Depending on the member's date of hire, MPSERS offers the option of participating in the defined contribution (DC) plan that provides a 50 percent employer match (up to 3 percent of salary) on employee contributions.

Members are eligible for nonduty disability benefits after 10 years of service and for duty-related disability benefits upon hire. Disability retirement benefits are determined in the same manner as retirement benefits, but are payable immediately without an actuarial reduction. The disability benefits plus authorized outside earnings are limited to 100 percent of the participant's final average compensation, with an increase of 2 percent each year thereafter.

Benefits may transfer to a beneficiary upon death and are determined in the same manner as retirement benefits, but with an actuarial reduction.

Benefit terms provide for annual cost of living adjustments to each employee's retirement allowance subsequent to the employee's retirement date. The annual adjustment, if applicable, is 3 percent. Some members who do not receive an annual increase are eligible to receive a supplemental payment in those years in which investment earnings exceed actuarial assumptions.

Note 10 - Michigan Public School Employees' Retirement System (Continued)

MPSERS provides medical, prescription drug, dental, and vision coverage for retirees and beneficiaries. A subsidized portion of the premium is paid by MPSERS, with the balance deducted from the monthly pension of each retiree healthcare recipient. Depending on the member's date of hire, this subsidized portion ranges from 80 percent to the maximum allowed by the statute.

Contributions

Public Act 300 of 1980, as amended, required the Agency to contribute amounts necessary to finance the coverage of pension benefits of active and retired members. Contribution provisions are specified by state statute and may be amended only by action of the state Legislature. Under these provisions, each school district's contribution is expected to finance the costs of benefits earned by employees during the year, with an additional amount to finance a portion of the unfunded accrued liability.

Under the OPEB plan, retirees electing this coverage contribute an amount equivalent to the monthly cost for Part B Medicare and 10 percent, or 20 percent for those not Medicare eligible, of the monthly premium amount for the health, dental, and vision coverage at the time of receiving the benefits. The MPSERS board of trustees annually sets the employer contribution rate to fund the benefits. Participating employers are required to contribute at that rate.

Under Public Act 300 of 2012, members were given the choice between continuing the 3 percent contribution to the retiree healthcare and keeping the premium subsidy benefit described above, or choosing not to pay the 3 percent contribution and instead opting out of the subsidy benefit and becoming a participant in the Personal Healthcare Fund (PHF), a portable, tax-deferred fund that can be used to pay healthcare expenses in retirement. Participants in the PHF are automatically enrolled in a 2 percent employee contribution into their 457 account as of their transition date, earning them a 2 percent employer match into a 401(k) account. Members who selected this option stop paying the 3 percent contribution to the retiree healthcare as of the day before their transition date, and their prior contributions were deposited into their 401(k) account.

The Agency's contributions are determined based on employee elections. There are multiple different pension and healthcare benefit options included in the plan available to employees based on date of hire and the elections available at that time. Contribution rates are adjusted annually by the ORS.

The range of rates is as follows:

| | Pension | OPEB |
|---------------------------------------|-----------------|---------------|
| October 1, 2017 - January 31, 2018 | 13.54% - 17.89% | 7.42% - 7.67% |
| February 1, 2018 - September 30, 2018 | 13.54% - 19.74% | 7.42% - 7.67% |

Depending on the plan selected, member pension contributions range from 0 percent up to 7.0 percent of gross wages. For certain plan members, a 4 percent employer contribution to the defined contribution pension plan is required. In addition, for certain plan members, a 3 percent employer match is provided to the defined contribution pension plan.

The Agency's required and actual pension contributions to the plan for the year ended June 30, 2018 were \$8,796,507, which include the Agency's contributions required for those members with a defined contribution benefit. The Agency's required and actual pension contributions include an allocation of \$3,190,869 in revenue received from the State of Michigan, and remitted to the System, to fund the MPSERS unfunded actuarial accrued liability (UAAL) stabilization rate for the year ended June 30, 2018. For the year ended June 30, 2018, the contributions also include a one-time payment to the Agency received under Section 147c(2) of the State Aid act, which the Agency then remitted as a contribution to the plan.

The Agency's required and actual OPEB contributions to the plan for the year ended June 30, 2018 were \$2,003,115, which include the Agency's contributions required for those members with a defined contribution benefit.

Note 10 - Michigan Public School Employees' Retirement System (Continued)

Net Pension Liability

At June 30, 2018, the Agency reported a liability of \$78,923,572 for its proportionate share of the net pension liability. The net pension liability was measured as of September 30, 2017, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of September 30, 2016, which used updated procedures to roll forward the estimated liability to September 30, 2017. The Agency's proportion of the net pension liability was based on a projection of its long-term share of contributions to the pension plan relative to the projected contributions of all participating reporting units, actuarially determined. At September 30, 2017 and 2016, the Agency's proportion was 0.304557 percent and 0.293470 percent, respectively.

Net OPEB Liability

At June 30, 2018, the Agency reported a liability of \$27,029,254 for its proportionate share of the net OPEB liability. The net OPEB liability for fiscal year 2018 was measured as of September 30, 2017, and the total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of September 30, 2016, which used updated procedures to roll forward the estimated liability to September 30, 2017. The Agency's proportion of the net OPEB liability was based on a projection of its long-term share of contributions to the OPEB plan relative to the projected contributions of all participating reporting units, actuarially determined. At September 30, 2017 and 2016, the Agency's proportion was 0.305227 percent.

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

For the year ended June 30, 2018, the Agency recognized pension expense of \$10,274,688, inclusive of payments to fund the MPSERS UAAL stabilization rate. At June 30, 2018, the Agency reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

| | Deferred Outflows of Resources | Deferred Inflows of Resources |
|---|--------------------------------------|----------------------------------|
| Difference between expected and actual experience | \$ 685,900 | \$ (387,261) |
| Changes in assumptions | 8,646,704 | - |
| Net difference between projected and actual earnings on pension plan investments | - | (3,773,066) |
| Changes in proportion and differences between the Agency's contributions and proportionate share of contributions | 5,096,336 | (11,319) |
| The Agency's contributions to the plan subsequent to the measurement date | 6,884,867 | - |
| Total | <u>\$ 21,313,807</u> | <u>\$ (4,171,646)</u> |

The \$3,190,869 reported as deferred inflows of resources resulting from the pension portion of state aid payments received pursuant to the UAAL payment will be recognized as state appropriations revenue for the year ending June 30, 2019. Amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

| Years Ending | Amount |
|--------------|----------------------|
| 2019 | \$ 3,531,948 |
| 2020 | 4,541,555 |
| 2021 | 2,045,940 |
| 2022 | 137,851 |
| Total | <u>\$ 10,257,294</u> |

June 30, 2018

Note 10 - Michigan Public School Employees' Retirement System (Continued)

In addition, the contributions subsequent to the measurement date will be included as a reduction of the net pension liability in the next year.

OPEB Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB

For the year ended June 30, 2018, the Agency recognized OPEB expense of \$1,808,640.

At June 30, 2018, the Agency reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

| | <u>Deferred Outflows of Resources</u> | <u>Deferred Inflows of Resources</u> |
|--|---|--|
| Difference between expected and actual experience | \$ - | \$ (287,782) |
| Net difference between projected and actual earnings on OPEB plan investments | - | (626,004) |
| Changes in proportionate share or difference between amount contributed and proportionate share of contributions | 3,215 | - |
| Employer contributions to the plan subsequent to the measurement date | <u>1,593,810</u> | <u>-</u> |
| Total | <u>\$ 1,597,025</u> | <u>\$ (913,786)</u> |

Amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows (note that employer contributions subsequent to the measurement date will reduce the net OPEB liability and, therefore, will not be included in future pension expense):

| <u>Years Ending</u> | <u>Amount</u> |
|---------------------|---------------------|
| 2019 | \$ (220,099) |
| 2020 | (220,099) |
| 2021 | (220,099) |
| 2022 | (220,099) |
| 2023 | <u>(30,175)</u> |
| Total | <u>\$ (910,571)</u> |

Actuarial Assumptions

The total pension liability and total OPEB liability as of September 30, 2017 is based on the results of an actuarial valuation as of September 30, 2016 and rolled forward. The total pension liability was determined using the following actuarial assumptions:

| | | |
|-------------------------------------|----------------|--|
| Actuarial cost method | | Entry age normal cost actuarial cost method |
| Investment rate of return - Pension | 7.00% - 7.50% | Net of investment expenses based on the groups |
| Investment rate of return - OPEB | 7.50% | Net of investment expenses based on the groups |
| Salary increases | 3.50% - 12.30% | Including wage inflation of 3.50% |
| Healthcare cost trend rate | 7.50% | Year 1 graded to 3.5% year 12 |
| Mortality basis | | RP2000 Combined Healthy Mortality Table, adjusted for mortality improvements to 2025 using projection scale BB |
| Cost of living pension adjustments | 3.00% | Annual noncompounded for MIP members |

Assumption changes as a result of an experience study for the periods from 2007 to 2012 have been adopted by the System for use in the annual pension valuations beginning with the September 30, 2014 valuation.

June 30, 2018

Note 10 - Michigan Public School Employees' Retirement System (Continued)

Discount Rate

The discount rate used to measure the total pension liability was 7.00 - 7.50 percent as of September 30, 2017 depending on the plan option. The discount rate used to measure the total OPEB liability was 7.50 percent as of September 30, 2017. The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current contribution rate and that district contributions will be made at statutorily required rates.

Based on those assumptions, the pension plan's fiduciary net position and the OPEB plan's fiduciary net position were projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan and OPEB plan investments was applied to all periods of projected benefit payments to determine the total pension liability and total OPEB liability.

The long-term expected rate of return on pension plan and OPEB plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

| Asset Class | Target Allocation | Long-term Expected Real Rate of Return |
|---|-------------------|--|
| Domestic equity pools | 28.00 % | 5.60 % |
| Private equity pools | 18.00 | 8.70 |
| International equity pools | 16.00 | 7.20 |
| Fixed-income pools | 10.50 | (0.10) |
| Real estate and infrastructure pools | 10.00 | 4.20 |
| Real return, opportunistic, and absolute pool | 15.50 | 5.00 |
| Short-term investment pools | 2.00 | (0.90) |
| Total | 100.00 % | |

MPSERS approved a decrease in the discount rate for the September 30, 2017 annual actuarial valuation for the pension plan and the OPEB plan to 7.05 percent and 7.15 percent, respectively. As a result, the actuarial computed employer contributions, the net pension liability, and net OPEB liability will increase for the measurement period ended September 30, 2018.

Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the Agency, calculated using the discount rate depending on the plan option. The following also reflects what the Agency's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower or 1 percentage point higher than the current rate:

| | 1 Percent Decrease (6.00 - 6.50%) | Current Discount Rate (7.00 - 7.50%) | 1 Percent Increase (8.00 - 8.50%) |
|-------------------------------------|---|--|---|
| Net pension liability of the Agency | \$ 102,811,164 | \$ 78,923,572 | \$ 58,811,742 |

June 30, 2018

Note 10 - Michigan Public School Employees' Retirement System (Continued)

Sensitivity of the Net OPEB Liability to Changes in the Discount Rate

The following presents the net OPEB liability of the Agency, calculated using the current discount rate. It also reflects what the Agency's net OPEB liability would be if it were calculated using a discount rate that is 1 percentage point lower or 1 percentage point higher than the current rate:

| | 1 Percent Decrease (6.50%) | Current Discount Rate (7.50%) | 1 Percent Increase (8.50%) |
|----------------------------------|----------------------------------|-------------------------------------|----------------------------------|
| Net OPEB liability of the Agency | \$ 31,659,069 | \$ 27,029,254 | \$ 23,099,991 |

Sensitivity of the Net OPEB Liability to Changes in the Healthcare Cost Trend Rate

The following presents the net OPEB liability of the School District, calculated using the current healthcare cost trend rate. It also reflects what the School District's net OPEB liability would be if it were calculated using a healthcare cost trend rate that is 1 percentage point lower or 1 percentage point higher than the current rate:

| | 1 Percent Decrease (6.50%) | Current Discount Rate (7.50%) | 1 Percent Increase (8.50%) |
|----------------------------------|----------------------------------|-------------------------------------|----------------------------------|
| Net OPEB liability of the Agency | \$ 22,890,145 | \$ 27,029,254 | \$ 31,728,924 |

Pension Plan and OPEB Plan Fiduciary Net Position

Detailed information about the plan's fiduciary net position is available in the separately issued MPSERS financial report.

Payable to the Pension Plan and OPEB Plan

At June 30, 2018, the Agency reported a payable of \$1,031,021 and \$194,416 for the outstanding amount of contributions to the pension plan and OPEB plan, respectively, required for the year ended June 30, 2018.

Note 11 - Tax Abatements

The Agency receives reduced property tax revenue as a result of Industrial Facilities Tax exemptions (PA 198 of 1974) and Brownfield Redevelopment Agreements granted by cities, villages, and townships within the boundaries of the Agency. Industrial facility exemptions are intended to promote construction of new industrial facilities or to rehabilitate historical facilities; Brownfield redevelopment agreements are intended to reimburse taxpayers that remediate environmental contamination on their properties.

For the fiscal year ended June 30, 2018, the Agency's property tax revenue was reduced by approximately \$1,995,000 under these programs.

The Agency is reimbursed for lost revenue caused by tax abatements on the operating millage of nonhomestead properties from the State of Michigan under the School Aid formula. The Agency received approximately \$947,000 in reimbursements from the State of Michigan. The Agency is not reimbursed for lost revenue from debt service millages, There are no abatements made by the Agency.

Required Supplemental Information

Kalamazoo Regional Educational Service Agency

Required Supplemental Information Budgetary Comparison Schedule - General Fund

Year Ended June 30, 2018

| | Original Budget | Final Budget | Actual | (Under) Over Final Budget |
|---|---------------------|---------------------|---------------------|------------------------------|
| Revenue | | | | |
| Local sources | \$ 15,308,541 | \$ 17,397,863 | \$ 15,923,746 | \$ (1,474,117) |
| State sources | 13,804,905 | 15,112,113 | 13,643,980 | (1,468,133) |
| Federal sources | 10,006,701 | 9,978,688 | 9,679,311 | (299,377) |
| Interdistrict sources | 5,812,820 | 6,054,457 | 6,023,302 | (31,155) |
| Total revenue | 44,932,967 | 48,543,121 | 45,270,339 | (3,272,782) |
| Expenditures | | | | |
| Current: | | | | |
| Instruction: | | | | |
| Basic programs | 4,809,752 | 4,759,360 | 4,725,869 | (33,491) |
| Added needs | 103,539 | 103,818 | 91,673 | (12,145) |
| Support services: | | | | |
| Pupil | 1,409,611 | 1,335,626 | 1,326,991 | (8,635) |
| Instructional staff | 5,120,871 | 5,883,421 | 5,295,366 | (588,055) |
| General administration | 513,391 | 524,327 | 521,548 | (2,779) |
| School administration | 382,295 | 383,499 | 383,437 | (62) |
| Business | 1,104,790 | 926,585 | 909,382 | (17,203) |
| Operations and maintenance | 1,053,428 | 1,204,565 | 1,178,588 | (25,977) |
| Pupil transportation services | 827,768 | 909,581 | 956,914 | 47,333 |
| Central | 7,226,292 | 8,572,707 | 7,448,721 | (1,123,986) |
| Community services | 4,375,359 | 5,854,690 | 4,114,998 | (1,739,692) |
| Intergovernmental transfers | 17,975,051 | 17,875,720 | 17,697,262 | (178,458) |
| Total expenditures | 44,902,147 | 48,333,899 | 44,650,749 | (3,683,150) |
| Other Financing Uses - Transfers out | (200,000) | (200,000) | (400,000) | (200,000) |
| Net Change in Fund Balance | (169,180) | 9,222 | 219,590 | 210,368 |
| Fund Balance - Beginning of year | 6,657,216 | 6,657,216 | 6,657,216 | - |
| Fund Balance - End of year | \$ 6,488,036 | \$ 6,666,438 | \$ 6,876,806 | \$ 210,368 |

Kalamazoo Regional Educational Service Agency

Required Supplemental Information Budgetary Comparison Schedule - Special Education Fund

Year Ended June 30, 2018

| | Original Budget | Final Budget | Actual | Over (Under) Final Budget |
|---|--------------------|-------------------|---------------------|------------------------------|
| Revenue | | | | |
| Local sources | \$ 34,889,476 | \$ 34,941,889 | \$ 34,994,062 | \$ 52,173 |
| State sources | 7,020,294 | 10,260,243 | 10,841,762 | 581,519 |
| Federal sources | 8,238,146 | 8,444,600 | 8,444,600 | - |
| Total revenue | 50,147,916 | 53,646,732 | 54,280,424 | 633,692 |
| Expenditures | | | | |
| Current: | | | | |
| Instruction - Added needs | 14,937,940 | 18,257,768 | 17,837,317 | (420,451) |
| Support services: | | | | |
| Pupil | 7,102,498 | 6,895,224 | 7,255,682 | 360,458 |
| Instructional staff | 3,150,419 | 3,189,654 | 3,143,333 | (46,321) |
| General administration | 182,051 | 184,611 | 184,360 | (251) |
| School administration | 116,007 | 138,725 | 127,744 | (10,981) |
| Business | 481,714 | 501,299 | 489,017 | (12,282) |
| Operations and maintenance | 1,732,555 | 1,832,093 | 1,790,900 | (41,193) |
| Pupil transportation services | 320,000 | 270,000 | 264,195 | (5,805) |
| Central | 1,547,491 | 1,567,449 | 1,598,556 | 31,107 |
| Intergovernmental transfers | 21,477,241 | 22,005,380 | 21,997,960 | (7,420) |
| Total expenditures | 51,047,916 | 54,842,203 | 54,689,064 | (153,139) |
| Other Financing Uses - Transfers out | (200,000) | - | (200,000) | (200,000) |
| Net Change in Fund Balance | (1,100,000) | (1,195,471) | (608,640) | 586,831 |
| Fund Balance - Beginning of year | 1,820,102 | 1,820,102 | 1,820,102 | - |
| Fund Balance - End of year | \$ 720,102 | \$ 624,631 | \$ 1,211,462 | \$ 586,831 |

Kalamazoo Regional Educational Service Agency

Required Supplemental Information Schedule of the Agency's Proportionate Share of the Net Pension Liability Michigan Public School Employees' Retirement System

Last Four Plan Years Plan Years Ended September 30

| | 2017 | 2016 | 2015 | 2014 |
|---|---------------|---------------|---------------|---------------|
| Agency's proportion of the net pension liability | 0.30456 % | 0.29347 % | 0.28589 % | 0.26398 % |
| Agency's proportionate share of the net pension liability | \$ 78,923,572 | \$ 73,217,461 | \$ 69,827,793 | \$ 58,145,605 |
| Agency's covered employee payroll | \$ 25,949,644 | \$ 25,305,032 | \$ 24,133,670 | \$ 21,982,381 |
| Agency's proportionate share of the net pension liability as a percentage of its covered employee payroll | 304.14 % | 289.34 % | 289.34 % | 264.51 % |
| Plan fiduciary net position as a percentage of total pension liability | 63.96 % | 63.01 % | 62.92 % | 66.20 % |

Kalamazoo Regional Educational Service Agency

Required Supplemental Information Schedule of Pension Contributions Michigan Public School Employees' Retirement System

Last Four Fiscal Years Years Ended June 30

| | 2018 | 2017 | 2016 | 2015 |
|--|----------------------|----------------------|----------------------|----------------------|
| Statutorily required contribution | \$ 8,196,468 | \$ 7,281,956 | \$ 6,836,654 | \$ 5,065,624 |
| Contributions in relation to the statutorily required contribution | 8,196,468 | 7,281,956 | 6,836,654 | 5,065,624 |
| Contribution Deficiency | \$ - | \$ - | \$ - | \$ - |
| Agency's Covered Employee Payroll | \$ 27,733,502 | \$ 26,591,414 | \$ 24,983,413 | \$ 23,143,913 |
| Contributions as a Percentage of Covered Employee Payroll | 29.55 % | 27.38 % | 27.36 % | 21.89 % |

Kalamazoo Regional Educational Service Agency

Required Supplemental Information Schedule of the Agency's Proportionate Share of the Net OPEB Liability Michigan Public School Employees' Retirement System

**Last One Plan Years
Plan Year Ended September 30**

| | <u>2017</u> |
|--|---------------|
| Agency's proportion of the net OPEB liability | 0.03523 % |
| Agency's proportionate share of the net OPEB liability | \$ 27,029,254 |
| Agency's covered employee payroll | \$ 25,949,644 |
| Agency's proportionate share of the net OPEB liability as a percentage of its covered employee payroll | 104.16 % |
| Plan fiduciary net position as a percentage of total OPEB liability | 36.53 % |

Kalamazoo Regional Educational Service Agency

Required Supplemental Information
Schedule of OPEB Contributions
Michigan Public School Employees' Retirement System

| | Last One Fiscal Year Year Ended June 30 |
|--|--|
| | <u>2018</u> |
| Statutorily required contribution | \$ 2,003,115 |
| Contributions in relation to the statutorily required contribution | <u>2,003,115</u> |
| Contribution Deficiency | <u>\$ -</u> |
| Agency's Covered Employee Payroll | \$ 27,733,502 |
| Contributions as a Percentage of Covered Employee Payroll | 7.22 % |

June 30, 2018

Budgetary Information

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for the General Fund and all special revenue funds, except that other financing uses include payments to other districts, principal and interest on long-term debt, and transfers to the capital projects fund. The budget statement differs from the presentation used in the fund-level statements due to the presentation of capital outlay amounts on a functional basis, along with other financing uses being included within expenditures. All annual appropriations lapse at fiscal year end.

Pension Information

Ultimately, 10 years of data will be presented in both of the pension-related schedules. The number of years currently presented represents the number of years since the accounting standard requiring these schedules first became applicable.

Benefit Changes

There were no changes of benefit terms for the plan year ended September 30, 2017.

Changes in Assumptions

On February 23, 2017, MPSERS approved a decrease in the discount rate for the September 30, 2016 annual actuarial valuation of 0.5 percent to 7.00 percent from 7.50 percent based on the group.

Covered Payroll

The employers' covered payroll to be reported in the required supplemental information is defined by GASB 82, *Pension Issues - an amendment to GASB Statements No. 67, No. 68, and No. 73*, as payroll on which contributions to a pension plan are based and by GASB 85, *Omnibus 2017*, as payroll on which contributions to the OPEB plan are based. For the Agency, covered payroll represents payroll on which contributions to both plans are based.

OPEB Information

Ultimately, 10 years of data will be presented in both of the OPEB-related schedules. The number of years currently presented represents the number of years since the accounting standard requiring these schedules first became applicable.

Benefit Changes

There were no changes of benefit terms for the plan year ended September 30, 2017.

Changes in Assumptions

There were no changes of benefit assumptions for the plan year ended September 30, 2017.

Covered Payroll

The employers' covered payroll to be reported in the required supplemental information is defined by GASB 82, *Pension Issues - an amendment to GASB Statements No. 67, No. 68, and No. 73*, as payroll on which contributions to a pension plan are based and by GASB 85, *Omnibus 2017*, as payroll on which contributions to the OPEB plan are based. For the Agency, covered payroll represents payroll on which contributions to both plans are based.

Other Supplemental Information

Kalamazoo Regional Educational Service Agency

Other Supplemental Information Combining Balance Sheet Nonmajor Governmental Funds

June 30, 2018

| | Debt Service Fund | Capital Project Funds | | Total |
|---|----------------------|--|--|---------------------|
| | | General Education Capital Projects Fund | Special Education Capital Projects Fund | |
| Assets | | | | |
| Cash and investments | \$ - | \$ 752,556 | \$ 1,076,347 | \$ 1,828,903 |
| Receivables - Property taxes receivable | 12,482 | - | - | 12,482 |
| Due from other funds | 569 | 200,000 | 200,000 | 400,569 |
| Restricted assets | 259,922 | - | - | 259,922 |
| Total assets | \$ 272,973 | \$ 952,556 | \$ 1,276,347 | \$ 2,501,876 |
| Liabilities - Accounts payable | \$ 122 | \$ 37,286 | \$ - | \$ 37,408 |
| Deferred Inflows of Resources | 11,774 | - | - | 11,774 |
| Total liabilities and deferred inflows of resources | 11,896 | 37,286 | - | 49,182 |
| Fund Balances | | | | |
| Restricted - Debt service | 261,077 | - | - | 261,077 |
| Committed - Building and site improvements | - | 915,270 | 1,276,347 | 2,191,617 |
| Total fund balances | 261,077 | 915,270 | 1,276,347 | 2,452,694 |
| Total liabilities, deferred inflows of resources, and fund balances | \$ 272,973 | \$ 952,556 | \$ 1,276,347 | \$ 2,501,876 |

Kalamazoo Regional Educational Service Agency

Other Supplemental Information Combining Statement of Revenue, Expenditures, and Changes in Fund Balances Nonmajor Governmental Funds

Year Ended June 30, 2018

| | Debt Service Fund | Capital Project Funds | | Total |
|--|----------------------|--|--|---------------------|
| | | General Education Capital Projects Fund | Special Education Capital Projects Fund | |
| Revenue | | | | |
| Local sources | \$ 2,731,507 | \$ 200,796 | \$ 14,468 | \$ 2,946,771 |
| State sources | 114,553 | - | - | 114,553 |
| Total revenue | 2,846,060 | 200,796 | 14,468 | 3,061,324 |
| Expenditures | | | | |
| Debt service: | | | | |
| Principal | 2,500,000 | - | - | 2,500,000 |
| Interest | 373,384 | - | - | 373,384 |
| Other | 60,105 | - | - | 60,105 |
| Capital outlay | - | 215,615 | - | 215,615 |
| Total expenditures | 2,933,489 | 215,615 | - | 3,149,104 |
| Excess of Revenue (Under) Over Expenditures | (87,429) | (14,819) | 14,468 | (87,780) |
| Other Financing Sources (Uses) | | | | |
| Face value of debt issued | 8,235,000 | - | - | 8,235,000 |
| Transfers in | - | 200,000 | 200,000 | 400,000 |
| Payment to bond refunding escrow agent | (8,177,635) | - | - | (8,177,635) |
| Total other financing sources | 57,365 | 200,000 | 200,000 | 457,365 |
| Net Change in Fund Balances | (30,064) | 185,181 | 214,468 | 369,585 |
| Fund Balances - Beginning of year | 291,141 | 730,089 | 1,061,879 | 2,083,109 |
| Fund Balances - End of year | \$ 261,077 | \$ 915,270 | \$ 1,276,347 | \$ 2,452,694 |

Kalamazoo Regional Educational Service Agency

**Other Supplemental Information
Schedule of Bonded Indebtedness**

June 30, 2018

| <u>Years Ending June 30</u> | <u>Kalamazoo Regional Educational Service Agency Principal</u> |
|-----------------------------|--|
| 2019 | \$ 2,710,000 |
| 2020 | 2,785,000 |
| 2021 | <u>2,590,000</u> |
| Total remaining payments | <u>\$ 8,085,000</u> |
| Principal payments due | May 1 and November 1 |
| Interest payments due | May 1 and November 1 |
| Interest rate | 1.78% |
| Original issue | <u>\$ 8,235,000</u> |