

Michigan Online School

**REPORT ON FINANCIAL STATEMENTS**  
(with required supplementary information)

Year ended June 30, 2018

Michigan Online School

**TABLE OF CONTENTS**

Independent Auditor’s Report..... 1

Management’s Discussion and Analysis..... 3

Basic Financial Statements

    School-wide Financial Statements

        Statement of Net Position..... 7

        Statement of Activities ..... 8

    Fund Financial Statements

        Governmental Funds

            Balance Sheet ..... 9

            Statement of Revenues, Expenditures and Changes  
                in Fund Balances..... 10

        Notes to Financial Statements ..... 11

Required Supplementary Information

    Budgetary Comparison Schedule—General Fund..... 19

## INDEPENDENT AUDITOR'S REPORT

Board of Directors  
Michigan Online School  
Gobles, Michigan

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the governmental activities and the general fund of Michigan Online School (the School), as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the School's basic financial statements as listed in the table of contents.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditor's Responsibility***

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

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

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

Board of Directors  
Michigan Online School  
Page 2

**Opinions**

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and the general fund of Michigan Online School as of June 30, 2018, and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

**Substantial Doubt about the School's Ability to Continue as a Going Concern**

The accompanying financial statements have been prepared assuming that the School will continue as a going concern. As discussed in Note B to the financial statements, the School was determined to not be in compliance with the pupil accounting rules that determine an eligible student to receive state school aid revenue. The School's eligible student count was reduced to zero and the School's state aid revenue for 2017-2018 was reduced to zero. Management's evaluation of the events and conditions and management's plans regarding those matters are also described in Note B. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

**Other Matters**

**Required Supplementary Information**

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on pages 3 through 6 and 19 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

**Other Reporting Required by Government Auditing Standards**

In accordance with *Government Auditing Standards*, we have also issued our report dated October 22, 2018, on our consideration of Michigan Online School's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of Michigan Online School's 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 Michigan Online School's internal control over financial reporting and compliance.



Muskegon, Michigan  
October 22, 2018

Michigan Online School  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
For the Year Ended June 30, 2018

This discussion and analysis of Michigan Online School's financial performance provides an overall review of the School's financial activities for the fiscal year ended June 30, 2018. The intent of this discussion and analysis is to provide, in layman's terms, a look at the School's performance and current position. We encourage readers to consider the information presented here in conjunction with the financial statements and the notes to the financial statements. Since this is Michigan Online School's first year of operations, there is no comparative information with the prior year.

This information is required by GASB 34 (Governmental Accounting Standards Board's Statement No. 34). GASB 34 requires the presentation of two basic types of financial statements; namely, School-wide Financial Statements and Fund Financial Statements.

**Overview of the Financial Statements**

This annual report consists of four parts: (1) the independent auditor's report, (2) management's discussion and analysis, (3) the basic financial statements, and (4) required supplementary information. The financial statements also include notes that explain some of the information in the statements and provide more detail data. The statements are followed by a section of required supplementary information that further explains and supports the financial statements with a comparison of the School's budget for the year.

**School-wide Financial Statements**

The school-wide statements provide a financial perspective of the School as a whole. These statements are on the "full accrual" basis of accounting and provide information about the School's overall financial status. They are used to help determine whether the School is better off or worse off as the result of the year's activities. There are two school-wide statements: the *Statement of Net Position* and the *Statement of Activities*.

The *Statement of Net Position* reports all of the School's assets, deferred inflows and outflows, and liabilities, both short-term and long-term, regardless if they are "currently available" or not. Capital assets and long-term obligations of the School are reported in this statement.

The *Statement of Activities* accounts for the current year's revenues and expenses regardless of when cash is received or paid. The intent of this statement is to summarize and simplify the information relative to funding received and expenditures made for School services.

The two school-wide statements report the School's net position and how they have changed. Net Position – the difference between the School's assets, deferred inflows and outflows, and liabilities – is one way to measure the School's financial health or position.

- Over time, increases or decreases in the School's net position are an indicator of whether its financial position is improving or deteriorating, respectively.
- To assess the School's overall health, one needs to consider additional non-financial factors such as the quality of the education provided.

In the school-wide statements, the School's activities are classified as *governmental activities*. This includes the School's basic services, such as regular and special education, transportation, and administration. State aid and federal grants typically finance most of these services.

Michigan Online School  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
 For the Year Ended June 30, 2018

**Fund Financial Statements**

The fund financial statements focus on individual parts of the School, reporting the School's operations in more detail than the school-wide statements. The fund level statements are reported on a *modified accrual basis*. Only those assets that are "*measurable*" and "*currently available*" are reported. Liabilities are recognized to the extent they are normally expected to be paid with current financial resources.

The fund statements are formatted to comply with the legal requirements of the Michigan Department of Education's "Accounting Manual." In the State of Michigan, the School's major instructional and instructional support activities are reported in the *General Fund*. The primary funding sources for the General Fund are typically from state foundation grant per student and state categorical funding for specific programs. The School has no other funds.

**Financial Analysis of the School as a Whole**

The net position of the School as of June 30, 2018, was approximately \$(2,644,000). Figure A-1 below shows a condensed breakdown of the net position.

**Figure A-1  
 Condensed Statement of Net Position**

<b>Governmental Activities</b>	
<b><u>2018</u></b>	
Current assets	\$ 854,320
<b>Total assets</b>	<b><u>854,320</u></b>
Current liabilities	3,498,521
<b>Total liabilities</b>	<b><u>3,498,521</u></b>
Net position	
Unrestricted	(2,644,201)
<b>Total net position</b>	<b><u><u>\$ (2,644,201)</u></u></b>

**Comments on Major Changes to Net Position**

The net position of the School decreased approximately \$(2,644,000) during the 2017-2018 year. Figure A-2 on the following page shows the breakdown of this change. The Statement of Activities presented later in the school-wide financial statements, provides greater detail on the School's annual activity. The cost of the School's governmental activities for the year was approximately \$2,644,000. The School had no state aid revenue in the current year due to an unfavorable pupil count audit. See Note B for more details.

Michigan Online School  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
 For the Year Ended June 30, 2018

**Figure A-2**

	<b>2018</b>
<b>Revenues</b>	\$ -
<b>Expenses</b>	
Instruction	880,643
Support services	1,763,558
<b>Total Expenses</b>	<b>2,644,201</b>
<b>Change in net position</b>	<b>(2,644,201)</b>
<b>Beginning net position</b>	-
<b>Ending net position</b>	<b>\$ (2,644,201)</b>

**Financial Analysis of the School's Funds**

The financial performance of the School as a whole is reflected in its governmental funds as well. The governmental funds equity decreased by approximately \$2,644,000 during the 2017-18 year. The General Fund equity ended the year at approximately \$(2,644,000). The primary factors affecting the School's governmental funds' fund balance are listed below.

*Factors Impacting Fund Equity*

- *Student enrollment* – Proposal A tied state aid funding to student enrollment. The School's student count on which our foundation allowance was based was zero students for the 2017-18 school year, as described in Note B.

**General Fund Budgetary Highlights**

The Uniform Budget Act of the State of Michigan requires that the Board of Directors approve the original budget for the upcoming fiscal year prior to July 1, the start of the fiscal year. When the budget is prepared each year, several unknown factors exist. Estimates are used for such major items as student count, service provider contracts, state aid, staffing, utilities, and repairs. As a matter of practice, the School amends its budget periodically during the year. These revisions are made in order to deal with unexpected changes in revenues and expenditures. The following analysis describes the reasons for changes in the budget during the year and the differences in actual and budget figures.

Michigan Online School  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
For the Year Ended June 30, 2018

**Original budget to final budget**

There was a 146% increase (\$1,666,129) in General Fund revenues from the original budget to the final budget.

- *State revenues* – enrollment was higher than originally budgeted.

There was a 93% increase (\$1,277,190) in General Fund expenditures from the original budget to the final budget.

- *Instruction and support services* – due to more students, operating costs were higher than originally budgeted.

**Final budget to actual**

There was a 100% difference (\$2,806,129) between the final revenue budget and the actual revenue.

- *State revenues* – the pupil count audit results were unfavorable and the School lost its state aid

There was less than a 1% difference (\$7,024) between the final expenditure budget and the actual expenditures.

- *School administration* – Budgeted more for superintendent wages

**Factors Bearing on the School's Future**

The decision on the appeal of the pupil count audit results as described in Note B will have a significant bearing on the School's ability to continue as a going concern.

The adopted budget for the 2018-19 fiscal year projects an increase in the fund balance of approximately \$578,000.

The budget will be amended during the year to reflect updated foundation allowance information, actual student counts, changes to any legislation, and final staffing assignments.

**Requests for Information**

This financial report is designed to provide the School's taxpayers, parents, students, investors and creditors with a general overview of the School's finances, and to show how the School is accountable for the money it receives. Questions concerning any of the information provided in this report, or requests for additional financial information should be addressed to the Michigan Online School, 209 S. State Street, PO Box 408, Gobles, MI 49055, telephone number (269) 216-6972.

Michigan Online School  
**STATEMENT OF NET POSITION**  
June 30, 2018

	<u><b>Governmental activities</b></u>
<b>ASSETS</b>	
Current assets	
Cash and cash equivalents	\$ 850,320
Prepaid items	4,000
Total assets	<u>854,320</u>
<b>LIABILITIES</b>	
Current liabilities	
Accounts payable and accrued liabilities	692,392
Due to other governmental units	2,806,129
Total liabilities	<u>3,498,521</u>
<b>NET POSITION</b>	
Unrestricted	<u>(2,644,201)</u>
Total net position	<u><u>\$ (2,644,201)</u></u>

The accompanying notes are an integral part of this statement.

Michigan Online School  
**STATEMENT OF ACTIVITIES**  
For the year ended June 30, 2018

<i>Functions/Programs</i>	<u>Expenses</u>	<u>Net (Expense) Revenue and Changes in Net Position Governmental activities</u>
Governmental activities		
Instruction	\$ 880,643	\$ (880,643)
Support services	1,763,558	(1,763,558)
Total governmental activities	<u>\$ 2,644,201</u>	(2,644,201)
Change in net position		(2,644,201)
Net position at beginning of year		<u>-</u>
Net position at end of year		<u>\$ (2,644,201)</u>

The accompanying notes are an integral part of this statement.

Michigan Online School  
**BALANCE SHEET**  
 Governmental Funds  
 June 30, 2018

	<b>General Fund</b>
<b>ASSETS</b>	
Cash and cash equivalents	\$ 850,320
Prepaid items	4,000
Total assets	<b>\$ 854,320</b>
 <b>LIABILITIES</b>	
Accounts payable	\$ 692,392
Due to other governmental units	2,806,129
Total liabilities	3,498,521
 <b>FUND BALANCES</b>	
Nonspendable - prepaid items	4,000
Unassigned	(2,648,201)
Total fund balances (deficit)	(2,644,201)
Total liabilities and fund balances (deficit)	<b>\$ 854,320</b>
 <b>NET POSITION OF GOVERNMENTAL ACTIVITIES</b>	 <b>\$ (2,644,201)</b>

The accompanying notes are an integral part of this statement.

Michigan Online School  
**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES**  
 Governmental Funds  
 For the year ended June 30, 2018

	<b>General Fund</b>
<b>REVENUES</b>	\$ -
<b>EXPENDITURES</b>	
Current	
Instruction	880,643
Support services	1,763,558
Total expenditures	2,644,201
Net change in fund balance	(2,644,201)
Fund balance at beginning of year	-
Fund balance at end of year	<b>\$ (2,644,201)</b>
 <b>CHANGE IN NET POSITION OF GOVERNMENTAL ACTIVITIES</b>	 <b>\$ (2,644,201)</b>

The accompanying notes are an integral part of this statement.

Michigan Online School  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018

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

The financial statements of Michigan Online School (School) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the School's accounting policies are described below.

**Reporting Entity**

The School is governed by an appointed five member Board of Directors (Board), which has responsibility and control over all activities related to public school education within the School. The School receives funding from local, state, and federal government sources and must comply with all of the requirements of these funding source entities.

Generally accepted accounting principles require that if the School is considered to be financially accountable for other organizations, those organizations should be included as component units in the School's financial statements. Since no organizations met this criterion, none are included in the financial statements.

**Basis of Presentation—Government-wide and Fund Financial Statements**

The government-wide financial statements (i.e., the Statement of Net Position and the Statement of Activities) report information on all of the nonfiduciary activities of the School. All fiduciary activities are reported only in the fund financial statements. Governmental activities normally are supported by intergovernmental revenues and other nonexchange transactions.

While separate government-wide and fund financial statements are presented, they are interrelated. The governmental activities column incorporates data from governmental funds. Separate financial statements are provided for governmental funds and fiduciary funds, even though the latter are excluded from the government-wide financial statements.

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

The fund financial statements provide information about the School's funds, including its fiduciary funds. Separate statements for each fund category – governmental and fiduciary – are presented. The emphasis of fund financial statements is on major governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

The School reports the following major governmental fund:

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

Michigan Online School  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018

**NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued**

**Measurement Focus and Basis of Accounting**

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as current financial resources or economic resources. The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

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

The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the School considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due. General capital asset acquisitions are reported as expenditures in governmental funds. Issuance of long-term debt and acquisitions under capital leases are reported as other financing sources.

State and federal aid, and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Expenditure-driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other eligibility requirements have been met and the amount is received during the period or within the availability period for this revenue source (within 60 days of year end).

The State of Michigan utilizes a foundation grant approach which provides for a specific annual amount of revenue per pupil based on a statewide formula. The foundation is funded from state and local sources. Revenues from state sources are primarily governed by the School Aid Act and the School Code of Michigan. The Michigan Department of Education administers the allocation of state funds to Schools based on information supplied by the Schools. For the current fiscal year, the foundation allowance was based on pupil membership counts taken in February.

The state portion of the foundation is provided primarily by a state education property tax millage of 6 mills on Principal Residence Exemption (PRE) property and an allocated portion of state sales and other taxes. The state revenue is recognized during the foundation period and is funded through payments from October to August. Thus, the unpaid portion at June 30 is reported as due from other governmental units.

The School also receives revenue from the state to administer certain categorical education programs. State rules require that revenue earmarked for these programs be used for its specific purpose. Certain governmental funds require an accounting to the state of the expenditures incurred. For categorical funds meeting this requirement, funds received and accrued, which are not expended by the close of the fiscal year are recorded as unearned revenue.

All other revenue items are considered to be measurable and available only when cash is received by the government.

Michigan Online School  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018

**NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued**

**Assets, Liabilities, Deferred Outflows/Inflows of Resources, and Net Position/Fund Balance**

***Cash and Investments***

The School's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

Investments for the School are reported at fair value (generally based on quoted market prices). Standards also provide that certain investments are valued at cost (or amortized cost) when they are of a short-term duration, the rate of return is fixed, and the School intends to hold the investment until maturity.

State statutes authorize the School to invest in bonds and other direct and certain indirect obligations of the U.S. Treasury; certificates of deposit, savings accounts, deposit accounts, or depository receipts of a bank, savings and loan association, or credit union, which is a member of the Federal Deposit Insurance Corporation, Federal Savings and Loan Insurance Corporation, or National Credit Union Administration, respectively; in commercial paper rated at the time of purchase within the three highest classifications established by not less than two standard rating services and which matures not more than 270 days after the date of purchase. The School is also authorized to invest in U. S. Government or federal agency obligation repurchase agreements, bankers' acceptances of U.S. banks, and mutual funds composed of investments as outlined above. The School's deposits and investments are in accordance with statutory authority.

***Inventories and Prepaid Items***

All inventories are valued at cost using the first-in/first-out method. The cost of such inventories is recorded as expenses when consumed rather than when purchased.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements. The cost of prepaid items is recorded as expenditures/expenses when consumed rather than when purchased.

***Net Position Flow Assumption***

Sometimes the government will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts of net position to report as restricted and unrestricted in the government-wide financial statements, a flow assumption must be made about the order in which the resources are considered to be applied.

It is the School's policy to consider restricted net position to have been depleted before unrestricted net position is applied.

***Fund Balance Flow Assumptions***

Sometimes the School will fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements a flow assumption must be made about the order in which the resources are considered to be applied. It is the School's policy to consider restricted fund balance to have been depleted before using any of the components of unrestricted fund balance. Further, when the components of unrestricted fund balance can be used for the same purpose, committed fund balance is depleted first, followed by assigned fund balance. Unassigned fund balance is applied last.

Michigan Online School  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018

**NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued**

**Assets, Liabilities, Deferred Outflows/Inflows of Resources, and Net Position/Fund Balance—Continued**

***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 government 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 School's highest level of decision-making authority. The Board of Directors is the highest level of decision-making authority for the School that can, by formal action prior to the end of the fiscal year, commit fund balance. Once adopted, the limitation imposed by formal action remains in place until a similar action is taken (another formal action) to remove or revise the limitation.

Amounts in the assigned fund balance classification are intended to be used by the School for specific purposes but do not meet the criteria to be classified as committed. The Board of Directors 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.

**Revenues and Expenditures/Expenses**

***Program Revenues***

Amounts reported as program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function or segment. Unrestricted state aid, interest and other internally dedicated resources are reported as general revenues rather than as program revenues.

**NOTE B—GOING CONCERN**

In June 2018, the School was notified that the results of the pupil count audit performed for the February 2018 count date concluded that no students were enrolled in full-time instructional courses as required by Michigan State Law and therefore the previously reported student count of 448 full-time equivalent (FTE) students was reduced to zero. State school aid is based on these FTE counts. For the 2018 fiscal year, the School anticipated receiving \$3,148,688 of state school aid revenue based on 448 FTEs funded at \$7,631 per FTE. Prior to the pupil count audit results the School had received \$2,806,129 of the anticipated state school aid revenue. That amount is now owed back to the Michigan Department of Education based on the pupil count audit results, leaving the School with no revenues for the year ended June 30, 2018.

Michigan Online School  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018

**NOTE B—GOING CONCERN—Continued**

The School has appealed the pupil count audit results to the Michigan Department of Education. The determination of the appeal is being held until the audited financial statements for June 30, 2018 are submitted to the Michigan Department of Education.

Due to the uncertainty and delay of the appeal decision, the School has also requested a repayment plan under MCL 388.1615(2) that would allow the School to repay the \$2,806,129 that is currently owed to the Michigan Department of Education over a period of up to nine years. This request is based on the hardship that would be caused by the School having to repay those funds immediately.

The School believes they can continue as a going concern if they are successful with the appeal of the pupil count audit results. If the pupil count audit results appeal is unsuccessful, but the School is approved for an extended repayment period, for the \$2,806,129 that would be owed to the Michigan Department of Education, the School believes they can continue as a going concern.

**NOTE C—STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY**

**Budgets and Budgetary Accounting**

Budgets are adopted on a basis consistent with accounting principles generally accepted in the United States of America. Annual appropriated budgets are adopted for the General Fund. All annual appropriations lapse at year end.

The School follows these procedures in establishing the budgetary data reflected in the financial statements:

1. Management submits to the Board of Directors a proposed operating budget for the fiscal year commencing on July 1. The operating budget includes proposed expenditures and the means of financing them. The level of control for the budgets is at the functional level as set forth and presented as required supplementary information.
2. Public hearings are conducted to obtain comments.
3. Prior to July 1, the budget is legally adopted by Board of Directors resolution pursuant to the Uniform Budgeting and Accounting Act (P.A. 621 of 1978). The Act requires that the budget be amended prior to the end of the fiscal year when necessary to adjust appropriations if it appears that revenues and other financing sources will be less than anticipated or so that expenditures will not be in excess of original estimates. Expenditures shall not be made or incurred, unless authorized in the budget, in excess of the amount appropriated. Violations, if any, in the General Fund are noted in the required supplementary information section.
4. Formal budgetary integration is employed as a management control device during the year.

The budget is amended during the year with supplemental appropriations, the last one approved prior to June 30, 2018.

Michigan Online School  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018

**NOTE C—STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY—Continued**

**Fund Deficits**

The Michigan State School Aid Act states a district receiving money under this act shall not adopt or operate under a deficit budget, and shall not incur an operating deficit in a fund during a school fiscal year. A school having an existing deficit or which incurs a deficit shall not be allotted or paid further sums under this act until the district submits to the Michigan Department of Education for approval a budget for the current fiscal year and a plan to eliminate the deficit not later than the end of the second fiscal year after the deficit was incurred. At June 30, 2018 the General Fund of the School had a deficit of \$2,644,201. The School will work with the Michigan Department of Education and submit any deficit elimination plans as required.

**NOTE D—DEPOSITS AND INVESTMENTS**

As of June 30, 2018, the School had no investments.

**Interest rate risk**

The School does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

**Credit risk**

State law limits investments in commercial paper and corporate bonds to the three highest classifications issued by nationally recognized statistical rating organizations. The School has no investment policy that would further limit its investment choices.

**Concentration of credit risk**

The School does not have a concentration of credit risk policy. Concentration of credit risk is the risk of loss attributed to the magnitude of the School investment in a single issuer, by diversifying the investment portfolio so that the impact of potential losses from any one type of security or issuer will be minimized.

**Custodial credit risk - deposits**

In the case of deposits, this is the risk that in the event of a bank failure, the School's deposits may not be returned to it. As of June 30, 2018, \$643,375 of the School's bank balance of \$895,960 was exposed to custodial credit risk because it was uninsured and uncollateralized.

**Custodial credit risk - investments**

The School does not have a custodial credit risk policy for investments. This is the risk that, in the event of the failure of the counterparty, the School will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party.

**Foreign currency risk**

The School is not authorized to invest in investments which have this type of risk.

Michigan Online School  
**NOTES TO FINANCIAL STATEMENTS**  
June 30, 2018

**NOTE E—COMMITMENTS AND CONTINGENCIES**

**Operating Lease**

The School has a building lease with an unrelated party with a current monthly rental of \$2,000 under a five-year lease, which expires October 2022. Expense for the year ended June 30, 2018 was approximately \$10,600. The lease also requires that certain occupancy expenses be paid by the lessee. The future minimum rental payments required under this operating lease are \$24,000 for years end 2019-2022 and \$8,000 for the year ended 2023.

**Grant Programs**

The School participates in grant programs, which are subject to program compliance audits by the grantor or its representatives. Such audits of these programs may be performed at some future date. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time although the School expects such amounts, if any, to be immaterial.

**NOTE F—OTHER INFORMATION**

**Risk Management**

The School is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; error and omissions; injuries to employees; and natural disasters. The School carries commercial insurance for risks of loss, including employee health and accident insurance. No settlements have occurred in excess of coverage for June 30, 2018 or any of the prior three years.

**Employee Services Agreement**

The School leases its employees from an employee leasing company and is not required to have these School employees covered by MPERS. Expenditures for employee costs such as salaries and wages, payroll taxes, and benefits under the management services agreements have been recorded and reported in conformance with the State of Michigan's standard chart of accounts.

**NOTE G—UPCOMING ACCOUNTING PRONOUNCEMENT**

GASB Statement 87—*Leases* was issued by the GASB in June 2017 and will be effective for the School's 2021 fiscal year. The objective of this Statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring 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, thereby enhancing the relevance and consistency of information about governments' leasing activities.

**REQUIRED SUPPLEMENTARY INFORMATION**

Michigan Online School  
**REQUIRED SUPPLEMENTARY INFORMATION**  
**BUDGETARY COMPARISON SCHEDULE**  
 General Fund  
 For the year ended June 30, 2018

	<u>Budgeted amounts</u>		<u>Actual</u>	<u>Variance with final budget- positive (negative)</u>
	<u>Original</u>	<u>Final</u>		
<b>REVENUES</b>				
State sources	\$ 1,140,000	\$ 2,806,129	\$ -	\$ (2,806,129)
Federal sources	126,667	-	-	-
Total revenues	1,266,667	2,806,129	-	(2,806,129)
<b>EXPENDITURES</b>				
Instruction				
Basic programs	208,333	799,998	797,310	2,688
Added needs	280,000	83,333	83,333	-
Support services				
Pupil	3,809	8,400	400	8,000
Instructional staff	-	289,974	289,974	-
General administration	38,000	332,742	354,874	(22,132)
School administration	158,550	372,507	354,065	18,442
Business	-	231,822	231,822	-
Operations and maintenance	647,781	43,154	43,128	26
Central	-	489,295	489,295	-
Facilities	37,562	-	-	-
Total expenditures	1,374,035	2,651,225	2,644,201	7,024
Excess (deficiency) of revenues over (under) expenditures	<u>\$ (107,368)</u>	<u>\$ 154,904</u>	(2,644,201)	<u>\$ (2,799,105)</u>
Fund balance at beginning of year			-	
Fund balance at end of year			<u>\$ (2,644,201)</u>	