

Detroit Innovation Academy

**Report to the Board of Directors
Year Ended June 30, 2014**

October 21, 2014

To the Board of Directors
Detroit Innovation Academy

We have recently completed our audit of the basic financial statements of Detroit Innovation Academy (the "Academy") as of and for the year ended June 30, 2014. In addition to our audit report, we are providing the following results of the audit, other recommendations, and informational items which impact the Academy:

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We are grateful for the opportunity to be of service to Detroit Innovation Academy. We would also like to extend our thanks to Michelle Kotas, Lisa Mullin, Ryan Cassette, and the entire business office for their assistance and preparedness during the audit. We recognize that preparing for the audit is carried out in addition to your staff's normal daily activities and appreciate the time and attention provided to us. Should you have any questions regarding the comments in this report, please do not hesitate to call.

Plante & Moran, PLLC

Results of the Audit

October 21, 2014

To the Board of Directors
Detroit Innovation Academy

We have audited the financial statements of Detroit Innovation Academy (the "Academy") as of and for the year ended June 30, 2014 and have issued our report thereon dated October 21, 2014. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under U.S. Generally Accepted Auditing Standards

As stated in our engagement letter dated April 9, 2014, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities. Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

As part of our audit, we considered the internal control of the Academy. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

Our audit of the Academy's financial statements has also been conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Under *Government Auditing Standards*, we are obligated to communicate certain matters that come to our attention related to our audit to those responsible for the governance of the Academy, including compliance with certain provisions of laws, regulations, contracts, grant agreements, certain instances of error or fraud, illegal acts applicable to government agencies, and significant deficiencies in internal control that we identify during our audit. Toward this end, we issued a separate letter dated October 21, 2014 regarding our consideration of the Academy's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our communication about planning matters dated August 20, 2014.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Academy are described in Note I to the financial statements.

No new accounting policies were adopted and the application of existing policies was not changed during the year ended June 30, 2014.

We noted no transactions entered into by the Academy during the year for which there is a lack of authoritative guidance or consensus.

We noted no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. There were no significant balances, amounts, or disclosures in the financial statements based on sensitive management estimates.

The disclosures in the financial statements are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

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

Disagreements with Management

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

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. We did not detect any misstatements as a result of audit procedures.

Significant Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, business conditions affecting the Academy, and business plans and strategies that may affect the risks of material misstatement with management each year prior to retention as the Academy's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition of our retention.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated October 21, 2014.

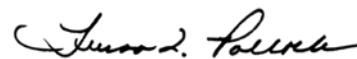
Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the Academy's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

This information is intended solely for the use of the board of directors and management of Detroit Innovation Academy and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

Plante & Moran, PLLC



Teresa L. Pollock

Other Recommendations

Detroit Innovation Academy

Other Recommendations

During our audit, we noted areas where there are opportunities for the Academy to further strengthen internal control or to improve operating practices. Our observations on those areas are presented for your consideration below.

- **Title I Accounting** - During testing of Title I, we noted the Academy tracks the grant expenditures in a separate Excel spreadsheet and then adjusts the general ledger periodically throughout the year when the reimbursement requests are made. Although this method of accounting for the grant is acceptable, we recommend more frequent reconciliation of Title I expenditures within the general ledger to support more frequent drawdowns of Title I funds. This would allow the Academy to maintain a higher level of liquidity.

In addition, we noted the general ledger budget detail was not updated to match the approved grant budget. While the approved grant budget was used to monitor the grant expenditures, we recommend the general ledger budget detail also be updated more frequently to allow the Academy to better monitor the grant expenditures.

We would also like to stress that the Academy should continue to ensure timekeeping documentation is in compliance with OMB Circular A-87, Attachment B, Item 8h.

- **Best Practice Funding** - During the past two fiscal years, the Academy has not been eligible to receive best practice funding. This funding was first built into the State School Aid Act in 2011-2012 and has continued through 2013-2014. To qualify for this funding for 2014-2015, the Academy would be required to meet seven of nine best practice initiatives. We recommend the Academy review the best practice requirements to determine if it could qualify for this additional funding in the current year.

Informational Items

State Aid Funding

State Aid and the Foundation Allowance - The fiscal year ended June 30, 2014 saw continued focus on several recurring themes in school funding by the State of Michigan: limited increases in the foundation allowance; additional funding boosts for districts/academies at the minimum foundation; additional resources dedicated to assisting with funding the districts'/academies' retirement/postretirement healthcare obligation (MPERS); and resources for best practice and student performance. While districts/academies experienced an increase in the foundation, the increases still have not replaced the \$470 per pupil cut experienced in 2011-2012.

2013-2014 Foundation: For the 2013-2014 fiscal year, the Academy's foundation allowance was increased to \$7,168. In the 2013-2014 State School Aid Act, a new funding provision was added (Section 20f). This section recognizes that the funding shift toward paying the growing MPERS expense could significantly harm some districts. Therefore, this categorical was added to guarantee at least a \$5 per pupil increase after giving account to the funding changes. Your academy's net increase exceeded the \$5 minimum and no additional funding was provided under this section.

2014-2015 Foundation: For the 2014-2015 fiscal year, the public school academy Maximum foundation allowance increases \$50, from \$7,168 to \$7,218. Additionally, the minimum foundation allowance rolls in the 2014 equity payment and increases by \$50 per pupil to \$7,126. Any academy receiving less than \$7,251 qualifies for up to a \$125 equity payment to move the funding level to \$7,251. No equity payments are provided if the 2014-2015 foundation allowance exceeds \$7,251. The equity payment is considered a one-time revenue source and is not required to be rolled into the 2015-2016 foundation allowance formula. Based on these changes, your Academy will receive a \$50 increase in its foundation allowance from \$7,168 to \$7,218, representing an increase of .7 percent. Additionally, your academy will receive a \$33 equity payment to bring the total per pupil funding to \$7,251. This represents a total increase from the 2013-2014 fiscal year of \$83.

Best Practice: Instead of mandating certain activities, the Governor identified many educational initiatives shortly after taking office and has used best practice funding to provide resources when an academy performs the identified activities. Each year, the list of criteria is modified and if an academy so chooses, it must meet the criteria in order to receive the funding. The amount provided in 2013-2014 was maintained at the same level as in 2012-2013 - \$52 per pupil. In 2013-2014, to qualify for this incentive, the Academy was required to meet seven of eight identified best practice initiatives. Because of the complexities of the requirements, your academy chose not to apply for the additional best practice funding. For 2014-2015, the per-pupil allocation was reduced to \$50/pupil and requires the Academy to meet seven of nine best practice criteria.

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Informational Items (Continued)

Performance Grants: In 2013-2014, academies could once again qualify for an additional categorical based on the Academy's ability to meet certain student performance measures. The maximum an academy could qualify for is \$100/pupil. For 2014-2015, performance funding continues. Depending on the Academy's student performance results, the Academy could receive one, two, or all three of the allocations of \$30/\$30/\$40 per pupil for performance measures. The measurement areas are grades 3-8 in reading, 3-8 in math, and 9-12 for all subjects tested, respectively.

Other State School Aid Act Changes Impacting 2014-2015

The Amendments to the State School Aid Act made several other changes impacting public school academies. Several changes we identified that could impact the Academy include:

Change in Academy Required Filing Dates - Currently the Academy must submit its audit report and its FID report to the Michigan Department of Education (MDE) by November 15. Beginning with the 2015 fiscal year, the reports will be due to the MDE on October 15. This significant acceleration will require academies and auditors to carefully plan the closing of the academy's books, and the completion of the audit and meetings with the Board of Directors to ensure the 2015 filing deadlines are met. There has continued to be legislative discussion as to whether October 15 is a realistic date for filing, but for now it is law, though a date of November 1 has been proposed within recent legislation. We will continue to keep you apprised of any changes in this area. Also included in this accelerated filing date is certain information related to student counts, which will impact your pupil accounting personnel.

Pupil Count Weighting - Academy membership blend will continue to be based on a 90/10 split. The funding is based on 90 percent of the October 2014 pupil count and 10 percent of the following February pupil count (February 2015). This means when the initial fiscal year budget is prepared, the Academy must estimate its foundation revenue using estimated student counts. In addition, if a student moves to another school after the October count date, the receiving school district or academy can claim a pro-rata share of the count with the "sending" district/academy having a like reduction. The tracking of students has become exponentially more complex and now involves reporting and coordination through the Intermediate School District and the State of Michigan. As a result, the actual student count, along with the actual foundation revenue, will not be finalized until near the end of the Academy's fiscal year.

At Risk Funding (31a) - For 2014-2015, there are several changes to the allowable uses of at-risk funds. The changes focus on third-grade reading proficiency and ensuring high school students are career/college ready. Academies will have to review at-risk programming to ensure use of funds aligns with these changes.

Great Start Readiness Program - Funding for 2014-2015 increased from \$65 million to \$130 million to provide up to 16,000 additional half-day slots for four-year-olds. The funds are provided to the Academy through the Intermediate School District. If the Academy is not participating in this program, this may be an opportunity to attract students to the Academy who could then remain in the Academy for their educational career.

Detroit Innovation Academy

Informational Items (Continued)

State Aid Planning Considerations for 2014-2015 and Beyond

Michigan's economy continues to improve. As we have seen by the Revenue Estimating Conference predictions, the School Aid Fund revenues are expected to grow, but at a slow pace. The governor's executive recommendations and legislative actions have provided some increases for general operations but have not replaced the \$470/pupil cut experienced several years ago. Increases are concentrated in early childhood and in funding for the increasing retirement obligation. While the final State School Aid Act amendments provided additional funds for operations in 2014-2015, the increase to the base foundation was actually lower than the governor's recommended increase of \$83/pupil. For academies above the minimum foundation, this lower increase may create the need to revisit revenue estimates used in the initial 2014-2015 budget. As the legislature and governor continue to modify tax policy and School Aid Fund resource allocations, the growth and availability of School Aid Fund resources to fund K-12 operations may be further limited.

Clearly, the key issue facing the future of school funding is the need to cover the cost of the retirement system. Because the costs continue to increase by amounts in excess of current contributions, the funding theme in the future will continue to be how to use School Aid Fund resources to cover the obligation. Funding this obligation will continue to impact the Academy's ability to receive additional resources to fund general education initiatives.

As the Academy looks to the future, careful planning will continue to be key. The use of budget modeling will increase in importance, especially as it looks to assess the impact of one-time funding resources on future funding projections. Given that many revenues are one-time resources, we recommend the Academy fully analyze the finances before entering into multi-year expenditure agreements.

New Rules Governing Management of Federal Programs

In December 2013, the Office of Management and Budget (OMB) issued long-awaited reforms to the compliance requirements that must be followed by nonfederal entities receiving federal funding. All academies receiving federal dollars will need to understand the changes made as a result of these reforms and may be required to make some changes to their internal procedures, processes, and controls.

These reforms impact three key areas of federal grants management:

- I. **Audit Requirements** - For fiscal years beginning on or after January 1, 2015 (fiscal year ending June 30, 2016 for Michigan schools), the threshold for obtaining a federal awards audit will increase from the current threshold of \$500,000 of annual federal spending to \$750,000. There will also be significant changes to the criteria for qualifying as a low-risk auditee and a reduction in the number of major programs required to be tested for some academies.

Detroit Innovation Academy

Informational Items (Continued)

2. **Cost Principles** - Effective December 26, 2014, the grant reforms related to cost principles go into effect. Not only were certain changes made to allowable costs under this new guidance, but there were significant changes in the area of time and effort reporting and indirect costs. The State of Michigan will have a significant impact on how these changes will be applied to Michigan schools, as they often have different requirements than the federal government in this area.
3. **Administrative Requirements** - Also effective December 26, 2014, nonfederal entities receiving federal funding must adhere to new rules related to administering federal awards. Most notably, these requirements may impact the Academy's procurement systems, including maintaining written conflict-of-interest policies and disclosures as well as updated grants management policies and procedures. The MDE has indicated that failure to adhere to these rules could result in the disqualification for participation in federal programs through the MDE. Please note these requirements are more stringent than those required under your federal program audit, which focuses on key controls versus overall process.

These revisions are clearly the most significant change to occur to federal grants management in recent history. Academies receiving federal funding will need to carefully digest these changes as the application of these changes will need to be assessed on an academy-by-academy basis. Plante & Moran, PLLC has many school district and public school academy grants experts in these rules who will be working closely with the Michigan Department of Education regarding these changes and can assist you in understanding the changes and how they impact the Academy. During the Spring of 2014, we provided two webinars on the grants management changes. Those webinars are archived and available at no charge on our website to assist academies in increasing their understanding of the changes. As we continue to delve into these new rules, we will keep you informed and updated.