

DEFIANCE CITY SCHOOL DISTRICT

DEFIANCE COUNTY, OHIO

AUDIT REPORT

For the Year Ended June 30, 2005

Charles E. Harris and Associates, Inc.
Certified Public Accountants and Governmental Consultants



**Auditor of State
Betty Montgomery**

Board of Education
Defiance City School District
629 Arabella Street
Defiance, Ohio 43512

We have reviewed the *Report of Independent Accountants* of the Defiance City School District, Defiance County, prepared by Charles E. Harris & Associates, Inc., for the audit period July 1, 2004 through June 30, 2005. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The Defiance City School District is responsible for compliance with these laws and regulations.

A handwritten signature in cursive script that reads "Betty Montgomery".

BETTY MONTGOMERY
Auditor of State

April 10, 2006

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**DEFIANCE CITY SCHOOL DISTRICT
AUDIT REPORT
For the Year Ended June 30, 2005**

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Charles E. Harris & Associates, Inc.
Certified Public Accountants

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REPORT OF INDEPENDENT ACCOUNTANTS

**Board of Education
Defiance City School District
629 Arabella St
Defiance, OH 43512**

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Defiance City School District, Defiance County, Ohio, (the District), as of and for the year ended June 30, 2005, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express an opinion 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 basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund and the aggregate remaining fund information of the Defiance City School District, Defiance County, Ohio, as of June 30, 2005, and the respective changes in financial position thereof and the budgetary comparison for the General Fund and for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As disclosed in Note 22 to the financial statements, the District implemented Governmental Accounting Standards Board (GASB) Technical Bulletin No. 2004-2, *Recognition of Pension and Other Postemployment Benefit Expenditures/Expenses and Liabilities by Cost-Sharing Employers* and GASB Statement No. 40, *Deposits and Investment Risk Disclosures*.

The management's discussion and analysis on pages 3 through 11 is not a required part of the basic financial statements, but is supplementary information the Governmental Accounting Standards Board requires. We have applied certain limited procedures, which consisted principally on inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 24, 2006 on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. While we did not opine on the internal control over financial reporting or on compliance, that report describes the scope of our testing of internal control over financial reporting and compliance and results of that testing. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*. You should read it in conjunction with this report in assessing the results of our audit.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Defiance City School District's basic financial statements. The accompanying schedule of federal awards expenditures is presented for the purposes of additional analysis as required by *U.S. Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. Such information as been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects, in relation to the basic financial statements taken as a whole.

Charles E. Harris & Associates, Inc.
February 24, 2006

Defiance City School District
Defiance County
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2005
(Unaudited)

The discussion and analysis of Defiance City School District's financial performance provides an overall review of the School District's financial activities for the fiscal year ended June 30, 2005. The intent of this discussion and analysis is to look at the School District's financial performance as a whole; readers should also review the basic financial statements and notes to enhance their understanding of the School District's financial performance.

Highlights

Highlights for fiscal year 2005 are as follows:

- In total, net assets decreased \$798,295, which represents an 8.04% decrease from 2004.
- General revenues accounted for \$19,700,962 in revenue or 89.08% of all revenues and reflect the School District's significant dependence on local property taxes, income taxes and unrestricted state entitlements.
- The District had \$22,915,550 in expenses related to governmental activities; only \$2,416,293 of these expenses was offset by program specific charges for services and sales, grants or contributions. General revenues supporting governmental activities (primarily taxes and unrestricted grants and entitlements) of \$19,700,962 were utilized to provide for these programs.
- The School District has received payments in lieu of taxes related to tax abatement agreements with several companies that are making capital investments in the School District. These payments have been placed into a permanent improvement fund. Revenues received in 2005 were \$51,205 and there were \$25,945 in expenditures. The Permanent Improvement Fund increased by \$25,260 during fiscal year 2005.
- The School District is part of the Northern Buckeye Educational Council Employee Insurance Benefits Program with member school districts located primarily in Defiance, Fulton, Henry, and Williams Counties. As with many health insurance plans, the School District's per policy health insurance premiums increased 21 percent in fiscal year 2005 and are decreasing by 24 percent in fiscal year 2006 due to negotiating a change in health insurance plans. This increase had a significant impact on the School District's budget and continues to be a major factor in fiscal decisions.

Using the Basic Financial Statements

This annual report consists of a series of financial statements and notes to those statements. The statements are organized so the reader can understand Defiance City School District as a financial whole, or as an entire operating entity.

The statement of net assets and the statement of activities provide information about the activities of the whole School District, presenting both an aggregate view of the School District's finances and a longer-term view of those finances.

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Defiance County
Management's Discussion and Analysis
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(Unaudited)

Fund financial statements provide a greater level of detail. For governmental funds, these statements tell how services were financed in the short-term as well as what remains for future spending. The fund financial statements also look at the School District's most significant funds, with all other non-major funds presented in total in a single column. For the Defiance City School District, the General Fund is the most significant fund.

Reporting the School District as a Whole

The statement of net assets and the statement of activities reflect how the School District did financially during fiscal year 2005. These statements include all assets and liabilities using the accrual basis of accounting similar to that which is used by most private-sector companies. This basis of accounting considers all of the current fiscal year's revenues and expenses regardless of when cash is received or paid.

These statements report the School District's net assets and changes in those assets. This change in net assets is important because it tells the reader whether the financial position of the School District as a whole has increased or decreased from the prior fiscal year. Over time, these increases and/or decreases are one indicator of whether the financial position is improving or deteriorating. Causes for these changes may be the result of many factors, some financial, some not. Non-financial factors include the School District's property tax base, current property tax laws in Ohio restricting revenue growth, facility conditions, required educational programs, and other factors.

In the statement of net assets and the statement of activities, the School District discloses a single type of activity, governmental activities. All of the School District's programs and services are reported here including instruction, support services, non-instructional services, and extracurricular activities.

Reporting the School District's Most Significant Funds

Fund financial statements provide detailed information about the School District's major funds. While the School District uses many funds to account for its financial transactions, the fund financial statements focus on the School District's most significant funds. The School District's only major governmental fund is the General Fund.

Governmental Funds - Most of the School District's activities are reported in governmental funds, which focus on how monies flow into and out of those funds and the balances left at fiscal year end for spending in future periods. These funds are reported using modified accrual accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund financial statements provide a detailed short-term view of the School District's general government operations and the basic services it provides. Governmental fund information helps determine whether there are more or less financial resources that can be spent in the near future to finance educational programs.

Fiduciary Funds - Fiduciary funds are used to account for resources held for the benefit of parties outside the School District. Fiduciary funds are not reflected on the government-wide financial statements because the resources from these funds are not available to support the School District's programs. These funds use the accrual basis of accounting.

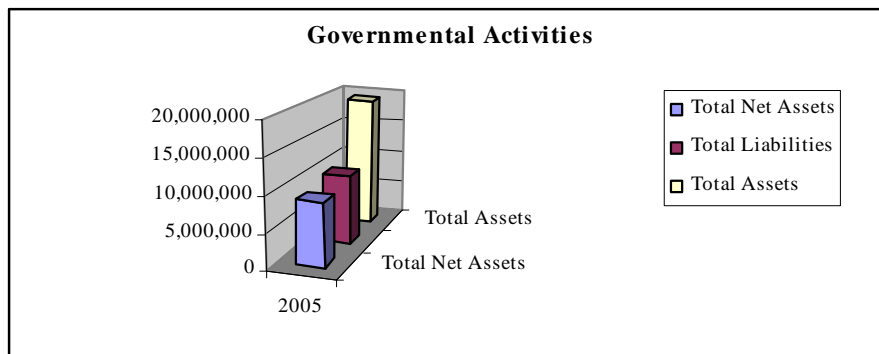
**Defiance City School District
Defiance County
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2005
(Unaudited)**

The School District as a Whole

Table 1 provides a summary of the School District's net assets for fiscal year 2005 compared to fiscal years 2004, 2003 and 2002:

Table 1
Net Assets

	<u>2005</u>	<u>2004</u>	<u>2003</u>	<u>2002</u>
<u>Assets:</u>				
Current and Other Assets	\$10,284,817	\$11,030,074	\$11,102,023	\$11,587,178
Capital Assets, Net	<u>8,840,216</u>	<u>9,166,519</u>	<u>9,156,378</u>	<u>9,072,700</u>
Total Assets	<u>19,125,033</u>	<u>20,196,593</u>	<u>20,258,401</u>	<u>20,659,878</u>
<u>Liabilities:</u>				
Current and Other Liabilities	8,372,908	8,591,820	7,780,151	7,873,507
Long-Term Liabilities	<u>1,625,729</u>	<u>1,680,082</u>	<u>1,901,432</u>	<u>2,041,545</u>
Total Liabilities	<u>9,998,637</u>	<u>10,271,902</u>	<u>9,681,583</u>	<u>9,915,052</u>
<u>Net Assets:</u>				
Invested in Capital Assets, Net of Related Debt	8,512,015	8,676,488	8,503,877	8,388,816
Restricted	1,547,977	1,353,729	1,168,822	1,510,753
Unrestricted	<u>(933,596)</u>	<u>(105,526)</u>	<u>904,119</u>	<u>845,257</u>
Total Net Assets	<u>\$9,126,396</u>	<u>\$9,924,691</u>	<u>\$10,576,818</u>	<u>\$10,744,826</u>



**Defiance City School District
Defiance County
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2005
(Unaudited)**

Total assets decreased \$401,477 from 2002 to 2003, \$61,808 from 2003 to 2004 and \$1,071,796 from 2004 to 2005. This reduction is less than 6 percent overall and is generally the result of lower cash balances in fiscal year 2004 and 2005. There is no particular individual asset account that had a great deal of fluctuation from the prior fiscal year.

At year-end, capital assets represented 46.23% of total assets. Capital assets include land, land improvements, buildings and improvements, furniture and equipment and vehicles. The amounts invested in capital assets net of related debt to acquire the assets at June 30, 2005, were \$8,514,432. These capital assets are used to provide services to the students and are not available for future spending. Although the District's investment in capital assets is reported net of related debt, it should be noted that the resources to repay the debt must be provided from other sources, since capital assets may not be used to liquidate these liabilities.

Total liabilities decreased by \$273,265 during fiscal year 2005 and increased by \$590,319 in fiscal year 2003. In 2003, the District combined the General Obligation Bonds and Energy Conservation Loan into one new loan to take advantage of lower interest rates.

The increase in invested in capital assets, net of related debt is the result principal payments made during the fiscal year reducing the outstanding debt applicable to capital assets.

A portion of the District's net assets, \$1,506,146 represents resources that are subject to external restriction on how they may be used.

Table 2 reflects the changes in net assets from fiscal year 2005, 2004 and 2003.

Table 2
Change in Net Assets
Governmental Activities

	<u>2005</u>	<u>2004</u>	<u>2003</u>
<u>Revenues</u>			
Program Revenues:			
Charges for Services	\$ 895,739	\$ 757,268	\$ 772,434
Operating Grants, Contributions, and Interest	1,520,554	1,780,278	2,153,705
Capital Grants and Contributions	0	0	45,206
Total Program Revenues	<u>\$ 2,416,293</u>	<u>\$ 2,537,546</u>	<u>\$ 2,971,345</u>

Defiance City School District
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Management's Discussion and Analysis
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(Unaudited)

Table 2
Change in Net Assets (continued)
Governmental
Activities

	2005	2004	2003
General Revenues:			
Property Taxes Levied for General Purposes	\$ 6,655,304	\$ 6,760,622	\$ 5,880,818
Income Taxes Levied for General Purposes	1,510,691	1,456,120	1,317,960
Payment in Lieu of Taxes	51,205	(16,718)	55,209
Grants and Entitlements	11,298,696	10,658,300	9,229,591
Interest	67,808	32,780	96,645
Extracurricular Activities	72,286	137,688	26,422
Rent	8,491	16,112	21,670
Miscellaneous	13,059	96,970	85,860
Loss on sale of Capital Assets	0	(6,955)	0
Proceeds from the Sale of Fixed Assets	0	3,728	0
Refund of Prior Year Expenditures/Receipts	23,422	0	0
Total General Revenues	<u>19,700,962</u>	<u>19,138,647</u>	<u>16,714,175</u>
Total Revenues	<u>22,117,255</u>	<u>21,676,193</u>	<u>19,685,520</u>
Instruction:			
Regular	9,132,804	8,986,278	9,106,831
Special	2,915,639	2,496,002	2,052,673
Vocational	280,861	267,931	227,709
Other	1,243,743	1,136,995	0
Support Services:			
Pupils	1,005,955	960,055	890,000
Instructional Staff	913,668	821,532	755,245
Board of Education	148,631	253,031	147,253
Administration	1,996,707	1,865,057	1,584,144
Fiscal	459,279	423,978	402,522
Operation and Maintenance of Plant	2,086,601	2,127,089	2,081,156
Pupil Transportation	892,664	710,764	648,938
Central	75,445	98,724	103,542
Non-Instructional Services	1,039,959	1,130,047	1,077,413
Extracurricular Activities	709,862	700,265	737,724
Capital Outlay	0	333,791	0
Interest and Fiscal Charges	13,732	16,781	38,378
Total Expenses	<u>22,915,550</u>	<u>22,328,320</u>	<u>19,853,528</u>
Decrease in Net Assets	<u>(\$ 798,295)</u>	<u>(\$ 652,127)</u>	<u>(\$ 168,008)</u>

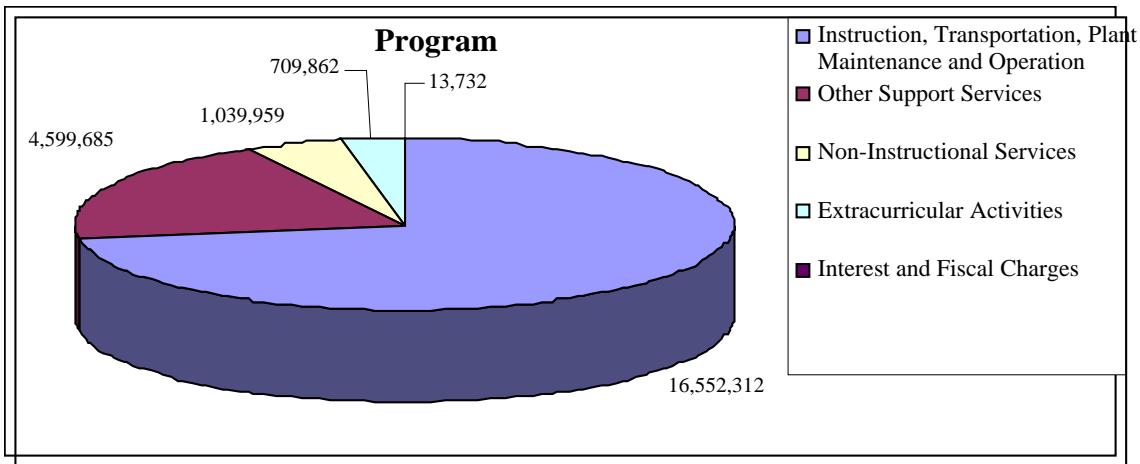
**Defiance City School District
Defiance County
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2005
(Unaudited)**

The net assets of the District's governmental activities decreased by \$798,295 or 8%. The total expenses of \$22,915,550 were offset by program revenues of \$2,416,293 and general revenues of \$19,700,962. Program revenues supported 10.93% of the total governmental expenses.

The primary sources of revenue for governmental activities are derived from property taxes, income taxes, grants and entitlements. These revenue sources represent 88.03% of total governmental revenue.

The major program expenses for governmental activities are for instruction, which accounts for 59.25% percent of all governmental expenses. Other programs which support the instruction process, including pupils, instructional staff, and pupil transportation account for 12.28% percent of governmental expenses. Maintenance of the School District's facilities also represents a significant expense, 9.09% percent. Therefore, 80.62% percent of the School District's expenses are related to the primary functions of providing facilities and delivering education.

The graph below presents the portion of the expenses, which are related directly to the District's primary functions.



Governmental Activities

Table 3 indicates the total cost of services and the net cost of services for governmental activities. The statement of activities reflects the cost of program services and the charges for services, grants, and contributions offsetting those services. The net cost of services identifies the cost of those services supported by tax revenues and unrestricted state entitlements. Comparisons can be made between fiscal year 2005, 2004 and 2003 figures.

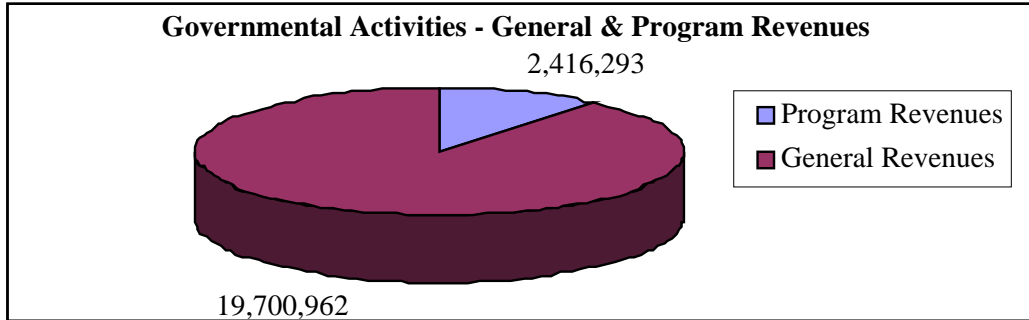
**Defiance City School District
Defiance County
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2005
(Unaudited)**

Table 3
Governmental Activities

	Total Cost of Services 2005	Net Cost of Services 2005	Total Cost of Services 2004	Net Cost of Services 2004	Total Cost of Services 2003	Net Cost of Services 2003
Instruction:						
Regular	\$9,132,804	\$8,754,190	\$9,202,518	\$8,816,957	\$9,106,831	\$8,643,620
Special	2,915,639	2,389,555	2,496,002	1,937,493	2,052,673	803,387
Vocational	280,861	280,578	267,931	267,689	227,709	226,663
Other	1,243,743	1,242,526	1,136,995	1,135,955	0	0
Support Services:						
Pupils	1,005,955	986,481	960,055	939,777	890,000	880,582
Instructional Staff	913,668	707,024	821,982	600,046	755,245	755,245
Board of Education	148,631	148,472	249,765	249,537	147,253	147,253
Administration	1,996,707	1,965,567	1,881,747	1,826,389	1,584,144	1,584,144
Fiscal	459,279	458,798	423,978	423,592	402,522	384,841
Operation and Maintenance of Plant	2,086,601	2,081,893	2,091,785	2,089,539	2,081,156	2,081,156
Pupil Transportation	892,664	886,154	822,654	804,121	648,938	579,582
Central	75,445	54,445	98,724	98,530	103,542	79,042
Non-Instructional Services	1,039,959	35,722	1,136,983	92,908	1,077,413	134,047
Extracurricular Activities	709,862	494,120	745,087	516,127	737,724	544,243
Capital Outlay	0	0	17,459	17,459	0	0
Interest and Fiscal Charges	13,732	13,732	17,632	17,632	38,378	38,378
Total Expenses	<u>\$22,915,550</u>	<u>\$20,499,257</u>	<u>\$22,371,297</u>	<u>\$19,833,751</u>	<u>\$19,853,528</u>	<u>\$16,882,183</u>

The dependence upon tax revenues and unrestricted state entitlements for governmental activities is demonstrated in the above table. Over 94 percent of instruction activities are supported through taxes and other general revenues. Over 97 percent of non-instructional services costs were covered by program revenues. This is primarily due to cafeteria sales, state and federal subsidies, and donated commodities for food service operations. Approximately 31 percent of extracurricular activities expenses are covered by program revenues. These program revenues are the result of music and athletic fees, ticket sales, and gate receipts at musical and athletic events.

**Defiance City School District
Defiance County
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2005
(Unaudited)**



The School District's Funds

The School District's governmental funds are accounted for using the modified accrual basis of accounting. Total governmental funds had revenues of \$21,921,224 in fiscal year 2005, \$21,730,792 in fiscal year 2004 and \$19,773,205 in 2003 and expenditures of \$22,645,620 in fiscal year 2005, \$22,432,861 in fiscal year 2004 and \$20,735,133 in 2003. The overall negative change for 2005 is \$724,396, or 31 percent, in fund balance for the fiscal year.

General Fund Budgeting Highlights

The School District's budget is prepared according to Ohio law and is based upon accounting for certain transactions on a basis of cash receipts, disbursements, and encumbrances. The most significant budgeted fund is the General Fund.

During fiscal year 2005, the School District amended its General Fund budget as needed. Final budgeted revenues, in the amount of \$19,673,917, were slightly above original budgeted revenues, in the amount of \$18,753,523. This difference is mostly due to unanticipated increases in property tax and state aide.

General fund original budgeted expenditures of \$19,264,489 were increased to \$20,620,645. The actual expenditures for fiscal year 2005 totaled \$20,064,189, which was \$556,456 less than the final budgeted expenditures.

Capital Assets and Debt Administration

Capital Assets

At the end of fiscal year 2005, the School District had \$8,840,216 invested in capital assets (net of accumulated depreciation), a decrease of \$326,303, or 4 percent from the prior years. For further information regarding the School District's capital assets, see Note 8 to the basic financial statements.

Defiance City School District
Defiance County
Management's Discussion and Analysis
For the Fiscal Year Ended June 30, 2005
(Unaudited)

Debt

The School District's outstanding debt obligations at fiscal year end consisted of an energy conservation loan, in the amount of \$297,500. The School District's long-term obligations also include compensated absences and a capital lease for equipment. For further information regarding the School District's long-term obligations, see Note 14 and 15 to the basic financial statements.

Current Issues

The Defiance City School's continues to responsibly budget dollars coming to the District. Perpetual challenges to the School District's financial outlook include the shortfalls in the state education budget, and aging facilities. Despite these challenges, the School District remains a strong service provider to the students of the Defiance area.

During fiscal year 2003, the Board of Education started receiving collections of revenues on a 5-year emergency levy, which was approved by voters in 2002. During the levy campaign, the Board and management informed citizens that the proposed levy would not provide adequate revenues for that five-year period of time and that a small levy would be needed to supplement the revenue stream sometime in year 3 or 4. The Board and management at this time indeed plan to place a levy on the ballot sometime in either in 2006 or 2007. The type and term and size of this levy are undecided at this time.

The community has always taken great pride in building and support of the District. In November 2005, the Board presented to the community, for the first attempt for approval, an OSFC proposal of constructing a new elementary building (K-4) and closing the four current elementaries. Voters strongly agreed and supported the project with the passage of the bond issue.

The Board of Education continues to aggressively market the School District to local and area students to increase enrollment. The Board looks forward to highlighting the many successful programs that the School District has to offer to young people in the Defiance area, which will result in additional revenue to the Defiance City Schools.

Contacting the School District's Financial Management

This financial report is designed to provide our citizens, taxpayers, investors, and creditors with a general overview of the School District's finances and to reflect the School District's accountability for the monies it receives. Questions concerning any of the information in this report or requests for additional information should be directed to Eric Beavers, CFO/Treasurer, Defiance City School District, 629 Arabella Street, Defiance, Ohio 43512.

Defiance City School District
Defiance County
Statement of Net Assets
June 30, 2005

	Governmental Activities
ASSETS	
Equity in Pooled Cash and Cash Equivalents	\$ 2,466,124
Cash and Cash Equivalents with Fiscal Agents	206
Receivables:	
Income Taxes	634,567
Property Taxes	6,692,052
Accounts	506
Accrued Interest	2,173
Intergovernmental	417,627
Prepaid Items	51,513
Inventory Held For Resale	20,049
Nondepreciable Capital Assets	1,004,940
Depreciable Capital Assets, Net	7,835,276
 <i>Total Assets</i>	 19,125,033
 LIABILITIES	
Accounts Payable	47,750
Accrued Wages and Benefits	1,929,166
Matured Compensated Absences Payable	15,670
Accrued Interest	3,285
Intergovernmental Payable	523,666
Deferred Revenue	5,853,371
Long-term liabilities:	
Due Within One Year	217,934
Due Within More Than One Year	1,407,795
 <i>Total Liabilities</i>	 9,998,637
 NET ASSETS	
Invested in Capital Assets, Net of Related Debt	8,512,015
Restricted for:	
Capital Projects	443,638
Debt Service	3,285
Other purposes	554,981
Set Asides	546,073
Unrestricted	(933,596)
 <i>Total Net Assets</i>	 \$ 9,126,396

See accompanying notes to the financial statements.

Defiance City School District
Defiance County
Statement of Activities
For the Fiscal Year Ended June 30, 2005

	Program Revenues		Net (Expense) Revenue and Changes in Net Assets	
Expenses	Charges for Services and Sales	Operating Grants and Contributions	Governmental Activities	
Governmental Activities				
Current:				
Instruction:				
Regular	\$ 9,132,804	\$ 9,420	\$ 369,194	\$ (8,754,190)
Special	2,915,639	2,107	523,977	(2,389,555)
Vocational	280,861	283	0	(280,578)
Other	1,243,743	1,217	0	(1,242,526)
Support services:				
Pupils	1,005,955	1,062	18,412	(986,481)
Instructional staff	913,668	759	205,885	(707,024)
Board of education	148,631	159	0	(148,472)
Administration	1,996,707	2,068	29,072	(1,965,567)
Fiscal	459,279	481	0	(458,798)
Operation and maintenance of plant	2,086,601	4,708	0	(2,081,893)
Pupil transportation	892,664	861	5,649	(886,154)
Central	75,445	0	21,000	(54,445)
Non-Instructional Services	1,039,959	722,364	281,873	(35,722)
Extracurricular activities	709,862	150,250	65,492	(494,120)
Debt service:				
Interest and fiscal charges	13,732	0	0	(13,732)
<i>Total Governmental Activities</i>	\$ 22,915,550	\$ 895,739	\$ 1,520,554	(20,499,257)

General Revenues

Property and Other Local Taxes	6,655,304
Income Taxes	1,510,691
Grants and Entitlements not Restricted to Specific Programs	11,298,696
Gifts and Donations	72,286
Investment Earnings	67,808
Rent	8,491
Miscellaneous	13,059
Payments in Lieu of Taxes	51,205
Refund of Prior Year Expenditures/Receipts	23,422
<i>Total General Revenues</i>	19,700,962
<i>Change in Net Assets</i>	(798,295)
<i>Net Assets Beginning of Year</i>	9,924,691
<i>Net Assets End of Year</i>	\$ 9,126,396

See accompanying notes to the financial statements.

Defiance City School District
Defiance County
Balance Sheet
Governmental Funds
June 30, 2005

	General	Other Governmental Funds	Total Governmental Funds
ASSETS			
Equity in Pooled Cash and Cash Equivalents	\$ 1,072,336	\$ 847,715	\$ 1,920,051
Cash and Cash Equivalents with Fiscal Agents	0	206	206
Receivables:			
Property Taxes	6,692,052	0	6,692,052
Income Taxes	634,567	0	634,567
Accounts	245	261	506
Accrued Interest	2,173	0	2,173
Intergovernmental	4,258	413,369	417,627
Interfund Receivable	65,629	0	65,629
Prepaid Items	51,513	0	51,513
Inventory Held For Resale	0	20,049	20,049
Restricted Assets:			
Equity in Pooled Cash and Cash Equivalents	546,073	0	546,073
Advances to Other Funds	68,000	0	68,000
Total Assets	\$ 9,136,846	\$ 1,281,600	\$ 10,418,446
LIABILITIES			
Accounts Payable	\$ 22,326	\$ 25,424	\$ 47,750
Accrued Wages and Benefits	1,741,166	188,000	1,929,166
Matured Compensated Absences Payable	15,670	0	15,670
Interfund Payable	0	65,629	65,629
Intergovernmental Payable	470,548	53,118	523,666
Deferred Revenue	5,969,423	208,899	6,178,322
Advances From Other Funds	0	68,000	68,000
Total Liabilities	8,219,133	609,070	8,828,203
FUND BALANCES			
Reserved			
Reserved for Encumbrances	117,225	120,620	237,845
Reserved for Inventory	0	20,049	20,049
Reserved for Prepaid Items	51,513	0	51,513
Reserved for Tax Revenue Unavailable for Appropriation	722,629	0	722,629
Reserved for Capital Improvements/Maintenance	546,073	0	546,073
Reserved for Advances	68,000	0	68,000
Unreserved, Undesignated, Reported in:			
General Fund	(587,727)	0	(587,727)
Special Revenue Funds	0	93,658	93,658
Capital Projects Funds	0	438,203	438,203
Total Fund Balances	917,713	672,530	1,590,243
Total Liabilities and Fund Balances	\$ 9,136,846	\$ 1,281,600	\$ 10,418,446

See accompanying notes to the financial statements.

Defiance City School District
Defiance County
Reconciliation of Total Governmental Fund Balances to
Net Assets Governmental Activities
June 30, 2005

Total Governmental Fund Balances	\$	1,590,243
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*Amounts reported for governmental activities in the
statement of net assets are different because:*

Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds		8,840,216
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Other long-term assets are not available to pay for current-period expenditures and therefore are deferred in the funds.

Federal and State Grants	\$ 208,899		
Delinquent Property Taxes	116,052		324,951

Some liabilities are not due and payable in the current period and therefore are not reported in the funds:

Accrued Interest Payable	(3,285)		
Compensated Absences	(1,297,528)		
Capital Lease Payable	(30,701)		
Notes Payable	(297,500)		(1,629,014)

<i>Net Assets of Governmental Activities</i>	\$	<u>9,126,396</u>
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See accompanying notes to the financial statements.

Defiance City School District
Defiance County
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds
For the Fiscal Year Ended June 30, 2005

	General	Other Governmental Funds	Total Governmental Funds
Revenues:			
Property and Other Local Taxes	\$ 6,668,032	\$ 0	\$ 6,668,032
Income Taxes	1,510,691	0	1,510,691
Intergovernmental	11,067,097	1,775,749	12,842,846
Investment income	63,295	4,513	67,808
Tuition and fees	6,958	81,953	88,911
Extracurricular activities	0	214,521	214,521
Rentals	8,491	822	9,313
Charges for services	14,057	415,364	429,421
Contributions and Donations	1,855	0	1,855
Payments in Lieu of Taxes	0	51,205	51,205
Miscellaneous	1,461	12,563	14,024
Total Revenues	19,341,937	2,556,690	21,898,627
Expenditures:			
Current:			
Instruction:			
Regular	8,625,792	415,296	9,041,088
Special	2,288,374	621,198	2,909,572
Vocational	276,426	0	276,426
Other	1,243,743	0	1,243,743
Support services:			
Pupils	951,812	34,908	986,720
Instructional staff	680,386	207,849	888,235
Board of education	148,599	0	148,599
Administration	1,912,195	51,030	1,963,225
Fiscal	448,584	0	448,584
Operation and maintenance of plant	2,006,200	2,687	2,008,887
Pupil transportation	774,346	6,005	780,351
Central	578	42,000	42,578
Operation of non-instructional services	34,244	981,129	1,015,373
Extracurricular activities	379,638	236,497	616,135
Capital outlay	88,125	10,000	98,125
Debt service:			
Principal retirement	13,855	148,750	162,605
Interest and fiscal charges	4,370	11,004	15,374
Total Expenditures	19,877,267	2,768,353	22,645,620
Excess of Revenues Over (Under) Expenditures	(535,330)	(211,663)	(746,993)
Other Financing Sources (Uses):			
Proceeds from sales of capital assets	140	0	140
Refund of Prior Year Expenditures/(Receipts)	23,422	(965)	22,457
Transfers in	0	159,754	159,754
Transfers out	(159,754)	0	(159,754)
Total Financing Sources and (Uses)	(136,192)	158,789	22,597
Net Change in Fund Balance	(671,522)	(52,874)	(724,396)
Fund balance at beginning of year	1,589,235	725,404	2,314,639
Fund balance at end of year	\$ 917,713	\$ 672,530	\$ 1,590,243

See accompanying notes to the financial statements.

Defiance City School District
Defiance County
Reconciliation of the Changes
in Fund Balances of Governmental Funds to the Statement of Activities
For the Fiscal Year Ended June 30, 2005

Net Change in Fund Balances - Total Governmental Funds \$ (724,396)

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, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which depreciation exceeded capital outlay in the current period.

Capital Asset Additions	\$ 255,323	
Current Year Depreciation	<u>(572,808)</u>	(317,485)

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.

Delinquent Property Taxes	(12,728)	
Intergovernmental Receivable	<u>257,978</u>	245,250

Net effect of transactions involving sale of capital assets are not reflected in the funds. (8,818)

Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets.

Note Principal	148,750	
Capital Leases	<u>13,855</u>	162,605

Some expenses reported in the statement of net activities such as pensions and compensated absences do not use the current financial resources and therefore are not reported as expenditures in governmental funds.

Accrued Interest	1,687	
Compensated Absences	(108,252)	
Pension Obligations	<u>(48,886)</u>	<u>(155,451)</u>

Change in Net Assets of Governmental Activities **\$ (798,295)**

Defiance City School District
Defiance County
Statement of Revenues, Expenditures, and Changes in Fund Balance -
Budget (Non-GAAP Basis) and Actual -
General Fund
For the Fiscal Year Ended June 30, 2005

	Budgeted Amounts			Variance with Final Budget Over (Under)
	Original	Final	Actual	
Revenues:				
Property and Other Local Taxes	\$ 6,584,454	\$ 6,953,711	\$ 6,597,583	\$ (356,128)
Income Taxes	1,408,849	1,469,331	1,469,331	0
Intergovernmental	10,658,022	11,127,142	11,062,839	(64,303)
Investment Income	42,545	60,545	62,346	1,801
Tuition and Fees	9,030	9,030	8,498	(532)
Rentals	19,337	19,337	8,491	(10,846)
Gifts and Donations		1,000	1,855	855
Charges for Services	10,568	10,568	14,057	3,489
Miscellaneous	20,718	23,253	3,697	(19,556)
Total Revenues	18,753,523	19,673,917	19,228,697	(445,220)
Expenditures:				
Current				
Instruction				
Regular	8,946,199	8,696,813	8,641,613	55,200
Special	1,988,894	2,337,220	2,240,638	96,582
Vocational	290,566	276,681	265,885	10,796
Other	847,446	1,251,504	1,246,119	5,385
Support Services				
Pupils	995,437	1,026,738	983,030	43,708
Instructional Staff	664,774	774,261	708,232	66,029
Board of Education	175,185	153,264	150,949	2,315
Administration	1,820,745	1,961,320	1,928,158	33,162
Fiscal	394,279	457,245	446,833	10,412
Operation and Maintenance of Plant	1,925,641	2,130,399	2,089,065	41,334
Pupil Transportation	721,405	863,579	815,573	48,006
Central	72,634	92,630	6,895	85,735
Operation of Non-Instructional Services	0	34,244	34,244	0
Capital Outlay	10,604	151,152	116,725	34,427
Extracurricular Activities	410,680	413,595	390,230	23,365
Total Expenditures	19,264,489	20,620,645	20,064,189	556,456
Excess of Revenues Over (Under) Expenditures	(510,966)	(946,728)	(835,492)	111,236
Other Financing Sources (Uses):				
Proceeds from Sale of Assets	3,765	3,765	140	(3,625)
Refund of Prior Year Expenditures	0	23,201	23,201	0
Advances In	7,070	7,070	0	(7,070)
Advances Out	(75,000)	(75,000)	(65,629)	9,371
Transfers Out	(81,514)	(159,754)	(159,754)	0
Total Other Financing Sources (Uses)	(145,679)	(200,718)	(202,042)	(1,324)
Excess of Revenues and Other Financing Sources Over (Under) Expenditures and Other Financing Uses	(656,645)	(1,147,446)	(1,037,534)	109,912
Fund Balance at Beginning of Year	2,459,612	2,459,612	2,459,612	0
Prior Year Encumbrances Appropriated	72,855	72,855	72,855	0
Fund Balance at End of Year	\$ 1,875,822	\$ 1,385,021	\$ 1,494,933	\$ 109,912

See accompanying notes to the financial statements.

Defiance City School District
Defiance County
Statement of Fiduciary Net Assets
Fiduciary Funds
June 30, 2005

	Private Purpose Trust	Agency Funds
Assets		
Equity in Pooled Cash and Cash Equivalents	\$ 10	\$ 75,525
Total Assets	10	75,525
 Liabilities		
Accounts Payable		131
Due to Students	0	75,394
Total Liabilities	0	75,525
 Net Assets		
Held in Trust for Scholarships	10	0
Total Net Assets	\$ 10	\$ 75,525

See accompanying notes to the financial statements.

Defiance City School District
Defiance County
Statement of Changes in Fiduciary Net Assets
Fiduciary Funds
June 30, 2005

	Private Purpose Trust
Additions	\$ 0
Deductions	0
<i>Change in Net Assets</i>	0
<i>Net Assets Beginning of Year</i>	10
<i>Net Assets End of Year</i>	\$ 10

See accompanying notes to the financial statements.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 1 – DESCRIPTION OF THE SCHOOL DISTRICT AND REPORTING ENTITY

Defiance City School District (the “School District”) is organized under Article VI, Sections 2 and 3 of the Constitution of the State of Ohio. The School District operates under a locally-elected Board form of government consisting of five members elected at-large for staggered four year terms. The School District provides educational services as authorized by state and federal guidelines.

The School District is the 196th largest in the State of Ohio (among 612 school districts) in terms of enrollment. It is staffed by one hundred twelve classified employees, one hundred ninety-two certified teaching personnel, and eighteen administrative employees who provide services to 2,536 students and other community members. The School District currently operates seven instructional/support buildings.

Reporting Entity

A reporting entity is composed of the primary government, component units, and other organizations that are included to insure the financial statements are not misleading. The primary government of the School District consists of all funds, departments, boards, and agencies that are not legally separate from the School District. For Defiance City School District, this includes general operations, food service, and student related activities of the School District.

Component units are legally separate organizations for which the School District is financially accountable. The School District is financially accountable for an organization if the School District appoints a voting majority of the organization’s governing board and (1) the School District is able to significantly influence the programs or services performed or provided by the organization; or (2) the School District is legally entitled to or can otherwise access the organization’s resources; the School District is legally obligated or has otherwise assumed the responsibility to finance the deficits of, or provide financial support to, the organization; or the School District is obligated for the debt of the organization. Component units may also include organizations that are fiscally dependent on the School District in that the School District approves the budget, the issuance of debt, or the levying of taxes. There are no component units of the Defiance City School District.

The School District’s reporting entity includes the following:

Non-Public Schools - Within the School District’s boundaries, the St John’s Catholic School, St. Mary’s Catholic School, St. John Lutheran School, and the Seventh Day Adventist School are operated as private schools. Current State legislation provides funding to the parochial schools. The monies are received and disbursed on behalf of the parochial schools by the Treasurer of the School District, as directed by the parochial schools. The activity is reflected in a special revenue fund of the School District.

The School District participates in six jointly governed organizations and two insurance pools. These organizations are the Northwest Ohio Computer Association, the Northern Buckeye Education Council, the Four County Career Center, the Northwestern Ohio Educational Research Council, Inc., the Northwest Ohio Special Education Regional Resource Center, the Northwest Ohio Regional Professional Development Center, the Northern Buckeye Education Council Employee Insurance Benefits Program, and the Northern Buckeye Education Council Workers’ Compensation Group Rating Plan. These organizations are presented in Notes 18 and 19 to the basic financial statements.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of Defiance City School District have been prepared in conformity with generally accepted accounting principles (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 School District also applies Financial Accounting Standards Board (FASB) statements and interpretations issued on or before November 30, 1989, to its governmental activities provided they do not conflict with or contradict GASB pronouncements. Following are the more significant of the School District's accounting policies.

A. Basis of Presentation

The School District's basic financial statements consist of government-wide financial statements, including a statement of net assets and a statement of activities, and fund financial statements, which provide a more detailed level of financial information.

Government-Wide Financial Statements

The statement of net assets and the statement of activities display information about the School District as a whole. These statements include the financial activities of the primary government, except for fiduciary funds.

The statement of net assets presents the financial condition of the governmental activities of the School District at fiscal year end. The statement of activities presents a comparison between direct expenses and program revenues for each program or function of the School District's governmental activities. Direct expenses are those that are specifically associated with a service, program, or department and, therefore, clearly identifiable to a particular function. Program revenues include charges paid by the recipient of the goods or services offered by the program and grants, contributions, and interest that are restricted to meeting the operational or capital requirements of a particular program. Revenues which are not classified as program revenues are presented as general revenues of the School District, with certain limited exceptions. The comparison of direct expenses with program revenues identifies the extent to which each governmental function is self-financing or draws from the general revenues of the School District.

Fund Financial Statements

During the fiscal year, the School District segregates transactions related to certain School District functions or activities in separate funds in order to aid financial management and to demonstrate legal compliance. Fund financial statements are designed to present financial information of the School District at this more detailed level. The focus of governmental fund financial statements is on major funds. Each major fund is presented in a separate column. Nonmajor funds are aggregated and presented in a single column. Fiduciary funds are reported by type.

B. Fund Accounting

The School District uses funds to maintain its financial records during the fiscal year. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts. The funds of the School District are divided into two categories, governmental and fiduciary.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Governmental Funds

Governmental funds are those through which most governmental functions of the School District are financed. Governmental fund reporting focuses on the sources, uses, and balances of current financial resources. Expendable assets are assigned to the various governmental funds according to the purposes for which they may or must be used. Current liabilities are assigned to the fund from which they will be paid. The difference between governmental fund assets and liabilities is reported as fund balance. The School District's only major fund is the General Fund.

General Fund - The General Fund is used to account for all financial resources, except those required to be accounted for in another fund. The General Fund balance is available to the School District for any purpose provided it is expended or transferred according to the general laws of Ohio.

The other governmental funds of the School District account for grants and other resources whose uses are restricted to a particular purpose.

Fiduciary Funds

Fiduciary fund reporting focuses on net assets and changes in net assets. The fiduciary fund category is split into four classifications: pension trust funds, investment trust funds, private purpose trust funds, and agency funds. Trust funds are used to account for assets held by the School District under a trust agreement for individuals, private organizations, or other governments and are not available to support the School District's own programs. The School District's private purpose trust fund accounts for college scholarships for students. Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. The School District's agency funds account for student athletic insurance, for amounts held to pay for college placement tests, and for various student-managed activities.

C. Measurement Focus

Government-Wide Financial Statements

The government-wide financial statements are prepared using a flow of economic resources measurement focus. All assets and all liabilities associated with the operation of the School District are included on the statement of net assets. The statement of activities presents increases (e.g., revenues) and decreases (e.g., expenses) in total net assets.

Fund Financial Statements

All governmental funds are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and current liabilities are generally included on the balance sheet. The statement of revenues, expenditures, and changes in fund balances reflects the sources (i.e., revenues and other financing sources) and uses (i.e., expenditures and other financing uses) of current financial resources. This approach differs from the manner in which the governmental activities of the government-wide financial statements are prepared. Governmental fund financial statements, therefore, include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the fund financial statements for governmental funds.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

D. Basis of Accounting

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. Governmental funds use the modified accrual basis of accounting; fiduciary funds use the accrual basis of accounting. Differences in the accrual and modified accrual basis of accounting arise in the recognition of revenue, the recording of deferred revenue, and in the presentation of expenses versus expenditures.

Revenues - Exchange and Nonexchange Transactions

Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On the modified accrual basis, revenue is recorded in the fiscal year in which the resources are measurable and become available. Available means the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year. For the School District, available means expected to be received within sixty days of fiscal year end.

Nonexchange transactions, in which the School District receives value without directly giving equal value in return, include property taxes, income taxes, grants, entitlements, and donations. On the accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from income taxes is recognized in the fiscal year in which the income is earned. Revenue from grants, entitlements, and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the fiscal year when the resources are required to be used or the fiscal year when use is first permitted; matching requirements, in which the School District must provide local resources to be used for a specified purpose; and expenditure requirements, in which the resources are provided to the School District on a reimbursement basis. On the modified accrual basis, revenue from nonexchange transactions must also be available before it can be recognized.

Under the modified accrual basis, the following revenue sources are considered both measurable and available at fiscal year end: property taxes available as an advance, income taxes, grants, interest, tuition, student fees, and charges for services, and rent.

Deferred Revenues

Deferred revenues arise when assets are recognized before revenue recognition criteria has been satisfied.

Property taxes for which there was an enforceable legal claim as of June 30, 2005, but which were levied to finance fiscal year 2006 operations, are recorded as deferred revenue. Grants and entitlements received before the eligibility requirements are met are also recorded as deferred revenue.

On governmental fund financial statements, receivables that will not be collected within the available period are reported as deferred revenue.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Expenses/Expenditures

On the accrual basis, expenses are recognized at the time they are incurred.

The measurement focus of governmental fund accounting is on decreases in net financial resources (expenditures) rather than expenses. Expenditures are generally recognized in the accounting period in which the related fund liability is incurred, if measurable. Allocations of cost, such as depreciation and amortization, are not recognized in governmental funds.

E. Budgetary Process

All funds, except agency funds, are legally required to be budgeted and appropriated. The major documents prepared are the tax budget, the certificate of estimated resources, and the appropriations resolution, all of which are prepared on the budgetary basis of accounting. The tax budget demonstrates a need for existing or increased tax rates. The certificate of estimated resources establishes a limit on the amount the Board of Education may appropriate. The appropriations resolution is the Board's authorization to spend resources and sets annual limits on expenditures plus encumbrances at the level of control selected by the Board. The legal level of budgetary control selected by the Board is at the function level for the General Fund and the fund level for all other funds. Any budgetary modifications at this level may only be made by resolution of the Board of Education. Budgetary allocations at the object level within the General Fund and at the function and object level within all other funds are made by the School District Treasurer.

The certificate of estimated resources may be amended during the fiscal year if projected increases or decreases in revenue are identified by the Treasurer. The amounts reported as the original budgeted amounts on the budgetary statements reflect the amounts on the certificate of estimated resources when the original appropriations were adopted. The amounts reported as the final budgeted amounts on the budgetary statements reflect the amounts on the amended certificate of estimated resources in effect at the time final appropriations were passed by the Board.

The appropriation resolution is subject to amendment throughout the fiscal year with the restriction that appropriations cannot exceed estimated resources. The amounts reported as the original budgeted amounts reflect the first appropriation resolution for that fund that covered the entire fiscal year, including amounts automatically carried forward from prior fiscal years. The amounts reported as the final budgeted amounts represent the final appropriation amounts passed by the Board during the fiscal year.

F. Cash and Investments

To improve cash management, cash received by the School District is pooled. Monies for all funds are maintained in this pool. Individual fund integrity is maintained through School District records. Interest in the pool is presented as "Equity in Pooled Cash and Cash Equivalents".

Cash and cash equivalents held for the School District by the Northwest Ohio Educational Service Center are reflected as "Cash and Cash Equivalents with Fiscal Agent".

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

During fiscal year 2005, investments included nonnegotiable certificates of deposit, US Treasury/Agency bonds and STAR Ohio. Nonnegotiable certificates of deposit are reported at cost. STAR Ohio is an investment pool, managed by the State Treasurer's Office, which allows governments within the State to pool their funds for investment purposes. STAR Ohio is not registered with the SEC as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in STAR Ohio are valued at STAR Ohio's share price, which is the price the investment could be sold for on June 30, 2005.

Following Ohio statutes, the Board of Education has, by resolution, specified the funds to receive an allocation of interest earnings. Total interest revenue credited to the District, on the accrual basis of accounting, during fiscal year 2005 was \$67,808. For the fund statements, \$63,295 interest was credited to the General Fund, and \$4,513 was recorded in non-major governmental funds.

Investments of the School District's cash management pool and investments with an original maturity of three months or less at the time they are purchased by the School District are presented on the financial statements as cash equivalents. Investments with an initial maturity of more than three months that were not purchased from the pool are reported as investments.

G. Prepaid Items

Payments made to vendors for services that will benefit periods beyond June 30, 2005, are recorded as prepaid items using the consumption method. A current asset for the prepaid amount is recorded at the time of purchase and an expenditure/expense is reported in the year in which services are consumed. At the fiscal year end, because prepayments are not available to finance future governmental fund expenditures, the fund balance is reserved on the fund financial statements by an amount equal to the carrying value of the assets.

H. Inventory

Inventory is presented at cost on a first-in, first-out basis and is expended/expensed when used. Inventory consists of donated and purchased food. On the fund financial statements, reported material and supplies inventory is equally offset by a fund balance reserve in the governmental funds which indicate that it does not constitute available spendable resources even though it is a component of net current assets.

I. Restricted Assets

Assets are reported as restricted when limitations on their use change the nature or normal understanding of the availability of the asset. Such constraints are either imposed by creditors, contributors, grantors, laws of other governments, or imposed by enabling legislation. Restricted assets in the General Fund represent amounts required by State statute to be set aside for the acquisition and construction of capital improvements.

J. Capital Assets

All of the School District's capital assets are general capital assets resulting from expenditures in governmental funds. These assets are reported in the governmental activities column on the government-wide statement of net assets but are not reported on the fund financial statements.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

All capital assets are capitalized at cost (or estimated historical cost) and updated for additions and reductions during the fiscal year. Donated capital assets are recorded at their fair market value on the date donated. The School District maintains a capitalization threshold of two thousand five hundred dollars. Improvements are capitalized. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset’s life are not capitalized.

All capital assets, except land, are depreciated. Improvements are depreciated over the remaining useful lives of the related capital assets. Depreciation is computed using the straight-line method over the following useful lives:

Description	Useful Lives
Land Improvements	10 – 50 years
Buildings and Building Improvements	10 – 118 years
Furniture, Fixtures and Equipment	4 – 40 years
Vehicles	8 – 15 years

K. Interfund Assets/Liabilities

On fund financial statements, receivables and payables resulting from short-term interfund loans or interfund services provided and used are classified as “Interfund Receivables/Payables”. Interfund balances within governmental activities are eliminated on the statement of net assets.

On fund financial statements, long-term interfund loans reported as “advances to/from other funds,” are equally offset by a fund balance reserve account which indicates that they do not constitute “available expendable financial resources” even though it is a component of net current assets. Repayment is expected to be made within a reasonable time.

L. Compensated Absences

Vacation benefits are accrued as a liability as the benefits are earned if the employees’ rights to receive compensation are attributable to services already rendered and it is probable the School District will compensate the employees for the benefits through time off or some other means. The School District records a liability for accumulated unused vacation time when earned for all employees with more than one year of service.

Sick leave benefits are accrued as a liability using the vesting method. The liability includes the employees who are currently eligible to receive termination benefits and those the School District has identified as probable of receiving payment in the future. The amount is based on accumulated sick leave and employees’ wage rates at fiscal year end, taking into consideration any limits specified in the School District’s termination policy. The School District records a liability for accumulated unused sick leave for all employees after twenty years of service and for all employees who have 15 years of service at age 45, 10 years of service at age 50, and 5 years of service at age 60.

The entire compensated absences liability is reported on the government-wide financial statements.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

On governmental fund financial statements, compensated absences are recognized as a liability and expenditure to the extent payments come due each period upon the occurrence of employee resignations and retirements. These amounts are recorded in the account “Matured Compensated Absences Payable” in the fund from which the employees who have accumulated unpaid leave are paid.

M. Accrued Liabilities and Long-Term Obligations

All payables, accrued liabilities, and long-term obligations are reported on the government-wide financial statements.

In general, governmental fund payables and accrued liabilities that, once incurred, are paid in a timely manner and in full from current financial resources are reported as obligations of the funds. However, compensated absences that are paid from governmental funds are reported as liabilities on the fund financial statements only to the extent that they are due for payment during the current year. Energy conservation loans and capital leases are recognized as a liability on the fund financial statements when due.

N. Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balance of any borrowing used for the acquisition, construction, or improvement of those assets. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the School District or through external restrictions imposed by creditors, grantors, or laws or regulations of other governments. Net assets restricted for other purposes include activities for food service operations, music and athletic programs, and federal and state grants restricted to expenditure for specified purposes.

The School District’s policy is to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

O. Fund Balance Reserves

The School District reserves those portions of fund balance which are legally segregated for a specific future use or which do not represent available expendable resources and, therefore, are not available for appropriation or expenditure. Unreserved fund balance indicates that portion which is available for appropriation in future periods. Fund balance reserves have been established for property taxes, prepaid items, inventory, advances, capital improvements, and encumbrances.

The reserve for property taxes represents taxes recognized as revenue under generally accepted accounting principles but not available for appropriation under State statute.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

P. Interfund Transactions

Transfers within governmental activities are eliminated on the government-wide financial statements.

Exchange transactions between funds are reported as revenues in the seller funds and as expenditures/expenses in the purchaser funds. Flows of cash or goods from one fund to another without a requirement for repayment are reported as interfund transfers. Interfund transfers are reported as other financing sources/uses in governmental funds. Repayments from funds responsible for particular expenditures/expenses to the funds that initially paid for them are not presented on the financial statements.

Q. Extraordinary and Special Items

Extraordinary items are transactions or events that are both unusual in nature and infrequent in occurrence. Special items are transactions or events that are within the control of management and are either unusual in nature or infrequent in occurrence.

R. Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

NOTE 3 - BUDGETARY BASIS OF ACCOUNTING

While the School District is reporting financial position, results of operations, and changes in fund balances on the basis of generally accepted accounting principles (GAAP), the budgetary basis as provided by law is based upon accounting for certain transactions on a basis of cash receipts, disbursements, and encumbrances. The Statement of Revenues, Expenditures, and Changes in Fund Balance - Budget (Non-GAAP Basis) and Actual for the General Fund is presented on the budgetary basis to provide a meaningful comparison of actual results with the budget. The major differences between the budget basis and the GAAP basis are as follows:

1. Revenues are recorded when received in cash (budget basis) as opposed to when susceptible to accrual (GAAP basis).
2. Expenditures are recorded when paid in cash (budget basis) as opposed to when the liability is incurred (GAAP basis).
3. Encumbrances are treated as expenditures (budget basis) rather than as a reservation of fund balance (GAAP basis).

**Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005**

NOTE 3 - BUDGETARY BASIS OF ACCOUNTING (continued)

The adjustments necessary to reconcile the GAAP and budgetary basis statements for the General Fund are as follows:

Net Change in Fund Balance	
GAAP Basis	\$ (671,522)
Adjustment for:	
Revenue accruals	(113,461)
Expenditure accruals	(83,813)
Prepaid items	(51,513)
Encumbrances outstanding at year-end	(117,225)
Budgetary Basis	\$ (1,037,534)

NOTE 4 – DEPOSITS AND INVESTMENTS

State statutes classify monies held by the School District into three categories.

Active deposits are public deposits necessary to meet current demands on the treasury. Such monies must be maintained either as cash in the School District Treasury, in commercial accounts payable or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts, or in money market deposit accounts.

Inactive deposits are public deposits the Board of Education has identified as not required for use within the current five year period of designation of depositories. Inactive deposits must either be evidenced by certificates of deposit maturing not later than the end of the current period of designation of depositories, or by savings or deposit accounts including, but not limited to, passbook accounts.

Interim deposits are deposits of interim monies. Interim monies are those monies which are not needed for immediate use but which will be needed before the end of the current period of designation of depositories. Interim deposits must be evidenced by time certificates of deposit maturing not more than one year from the date of deposit, or by savings or deposit accounts, including passbook accounts.

Interim monies may be deposited or invested in the following securities:

1. United States Treasury bills, bonds, notes, or any other obligation or security issued by the United States Treasury, or any other obligation guaranteed as to principal and interest by the United States;
2. Bonds, notes, debentures, or any other obligation or security issued by any federal government agency or instrumentality including, but not limited to, the Federal National Mortgage Association, Federal Home Loan Bank, Federal Farm Credit Bank, Federal Home Loan Mortgage Corporation, Government National Mortgage Association, and Student Loan Marketing Association. All federal agency securities shall be direct issuances of federal government agencies or instrumentalities;
3. Written repurchase agreements in the securities listed above provided the market value of the securities subject to the repurchase agreement must exceed the principal value of the agreement by at least 2 percent and be marked to market daily, and the term of the agreement must not exceed thirty days;

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 4 – DEPOSITS AND INVESTMENTS (continued)

4. Bonds and other obligations of the State of Ohio;
5. No-load money market mutual funds consisting exclusively of obligations described in division (1) or (2) and repurchase agreements secured by such obligations, provided that investments in securities described in this division are made only through eligible institutions; and
6. The State Treasurer's investment pool (STAR Ohio).
7. Certain bankers' acceptances and commercial paper notes for a period not to exceed one hundred and eighty days in an amount not to exceed twenty-five percent of the interim moneys available for investment at any one time.
8. Under limited circumstances corporate debt interest rated in either of the two highest rated classifications by at least two nationally recognized rating agencies.

Investments in stripped principal or interest obligations, reverse repurchase agreements, and derivatives are prohibited. The issuance of taxable notes for the purpose of arbitrage, the use of leverage, and short selling are also prohibited. An investment must mature within five years from the date of purchase, unless matched to a specific obligation or debt of the School District, and must be purchased with the expectation that it will be held to maturity.

Investments may only be made through specified dealers and institutions. Payment for investments may be made only upon delivery of the securities representing the investments to the Treasurer or qualified trustee or, if the securities are not represented by a certificate, upon receipt of confirmation of transfer from the custodian.

Protection of the School District's deposits is provided by the Federal Deposit Insurance Corporation (FDIC), by eligible securities pledged by the financial institution as security for repayment, by surety company bonds deposited with the Treasurer by the financial institution, or by a single collateral pool established by the financial institution to secure the repayment of all public monies deposited with the institution.

At fiscal year end, the School District had \$206 in cash and cash equivalents held by the Northwest Ohio Educational Service Center, which is presented as "Cash and Cash Equivalents with Fiscal Agent". The Educational Service Center holds this flow through grant money for the School District together with that of other school districts, and therefore, the School District cannot classify this money by risk.

Deposits

Custodial credit risk is the risk that in the event of bank failure, the government's deposits may not be returned to it. Protection of District cash and deposits is provided by the federal deposit insurance corporation as well as qualified securities pledged by the institution holding the assets. By law, financial institutions must collateralize all public deposits. The face value of the pooled collateral must equal at least 105 percent of public funds deposited. Collateral is held by trustees including the Federal Reserve Bank and designated third party trustees of the financial institutions.

**Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005**

NOTE 4 – DEPOSITS AND INVESTMENTS (continued)

At year end, the carrying amount of the District’s deposits was \$(196,141) and the bank balance was \$259,898. Of the bank balance, \$100,000 was covered by federal depository insurance and \$447,864 was uninsured and uncollateralized. Of the remaining uninsured bank balance, \$447,864 was collateralized with securities held by the pledging institution’s trust department not in the District’s name. The negative carrying amount above was due to the District investing in an overnight repurchase agreement described below.

Investments

Investments are reported at fair value. As of June 30, 2005, the District had the following investments:

	Fair Value	% of Total	Maturity (Years)	
			< 1	1-2
FHLMC	\$ 562,902	20.6	\$ 562,902	\$ 0
FHLB	501,051	18.3	501,051	0
FFCB	248,296	9.1	248,296	0
FNMA	950,531	34.7	598,226	352,305
STAR Ohio	187,024	6.8	187,024	0
Repurchase agreement	287,966	10.5	287,966	0
Total Fair Value	<u>\$ 2,737,770</u>	<u>100.0</u>	<u>\$ 2,385,465</u>	<u>\$ 352,305</u>

Interest Rate Risk

The Ohio Revised Code generally limits security purchases to those that mature within five years of the settlement date. The District’s policy indicates that the investments must mature within five years, unless matched to a specific obligation or debt of the District.

Credit Risk

The District’s investments at June 30, 2005 in FHLB, FNMA, FFCB, FHLMC and the repurchase agreement are rated AAA by Standard & Poor’s. Its investments Star Ohio is rated AAAM by Standard & Poor’s.

Concentration of Credit Risk

The District places no limit on the amount the District may invest in any one issuer. More than 5 percent of the District’s investments are in FHLMC, FHLB, FFCB, FNMA, STAR Ohio and the repurchase agreement. These investments are 20.6%, 18.3%, 9.1%, 34.7%, 6.8% and 10.5, respectively, of the District’s total investments, for the amounts listed above.

NOTE 5 - RECEIVABLES

Receivables at June 30, 2005, consisted of accounts (student fees and billings for user charged services), accrued interest, intergovernmental, income taxes, and property taxes. All receivables are considered collectible in full due to the ability to foreclose for the nonpayment of taxes, the stable condition of State programs, and the current year guarantee of federal funds. All receivables are expected to be collected within one year.

**Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005**

NOTE 5 – RECEIVABLES (continued)

A summary of the principal items of intergovernmental receivables follows:

	June 30, 2005
Governmental Activities	
General Fund	\$ 4,258
Other Governmental Funds:	
DPIA	7,530
Alternative Education	4,850
Special Education, Part B-IDEA	302,645
Title I	83,846
Innovative Programs, Title V	4,167
Technology, Title II-D	6,841
Drug Free	3,490
Total Intergovernmental Receivables	\$ 417,627

NOTE 6 – INCOME TAXES

The School District levies a voted tax of .5 percent for general operations on the income of residents and of estates. The tax was effective on January 1, 1991, and is a continuing tax. Employers of residents are required to withhold income tax on compensation and remit the tax to the State. Taxpayers are required to file an annual return. The State makes quarterly distributions to the School District after withholding amounts for administrative fees and estimated refunds. Income tax revenue is credited to the General Fund.

NOTE 7 – PROPERTY TAXES

Property taxes are levied and assessed on a calendar year basis, while the School District’s fiscal year runs from July through June. First-half tax distributions are received by the School District in the second half of the fiscal year. Second-half tax distributions are received in the first half of the following fiscal year.

Property taxes include amounts levied against all real property, public utility property, and tangible personal (used in business) property located in the School District. Real property tax revenues received in calendar year 2005 represent the collection of calendar year 2004 taxes. Real property taxes received in calendar year 2005 were levied after April 1, 2004, on the assessed values as of January 1, 2004, the lien date. Assessed values for real property taxes are established by State statute at 35 percent of appraised market value. Real property taxes are payable annually or semiannually. If paid annually, payment is due December 31; if paid semiannually, the first payment is due December 31, with the remainder payable by June 20. Under certain circumstances, State statute permits alternate payment dates to be established.

Public utility property tax revenues received in calendar year 2005 represent the collection of calendar year 2004 taxes. Public utility real and tangible personal property taxes received in calendar year 2005 became a lien on December 31, 2004, were levied after April 1, 2004, and are collected with real property taxes. Public utility real property is assessed at 35 percent of true value; public utility tangible personal property is currently assessed at varying percentages of true value.

**Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005**

NOTE 7 – PROPERTY TAXES (continued)

Tangible personal property tax revenues received in calendar year 2005 (other than public utility property) represent the collection of calendar year 2005 taxes. Tangible personal property taxes received in calendar year 2005 were levied after April 1, 2004, on the value as of December 31, 2004. Tangible personal property is currently assessed at 25 percent of true value for capital assets and 24 percent for inventory. Amounts paid by multi-county taxpayers are due September 20. Single county taxpayers may pay annually or semiannually. If paid annually, payment is due April 30; if paid semiannually, the first payment is due April 30, with the remainder payable by September 20. Tangible personal property taxes paid by April 30 are usually received by the School District prior to June 30.

The School District receives property taxes from Defiance and Paulding Counties. The County Auditors periodically advance to the School District its portion of the taxes collected. Second-half real property tax payments collected by the counties by June 30, 2005, are available to finance fiscal year 2005 operations. The amount available to be advanced can vary based on the date the tax bills are sent.

Accrued property taxes receivable represents real property, public utility property, and tangible personal property taxes which were measurable as of June 30, 2005, and for which there was an enforceable legal claim. Although total property tax collections for the next fiscal year are measurable, only the amount of real property taxes available as an advance at June 30 was levied to finance current fiscal year operations and is reflected as revenue at fiscal year end. The portion of the receivable not levied to finance current fiscal year operations is offset by a credit to deferred revenue.

The amount available as an advance at June 30, 2005, was \$722,629 in the General Fund.

On a full accrual basis, collectible delinquent property taxes have been recorded as a receivable and revenue. On a modified accrual basis, the revenue has been deferred.

The assessed values upon which fiscal year 2005 taxes were collected are:

	2004 Second-Half Collections		2005 First-Half Collections	
	<u>Amount</u>	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>
Agricultural/Residential	\$ 164,124,770	69.58%	\$ 166,015,260	69.36%
Industrial/Commercial	33,986,320	14.41%	34,961,040	14.61%
Public Utility	11,168,310	4.74%	11,904,180	4.97%
Tangible Personal Property	<u>26,592,934</u>	<u>11.27%</u>	<u>26,455,638</u>	<u>11.06%</u>
Total Assessed Value	<u>\$ 235,872,334</u>	<u>100.00%</u>	<u>\$ 239,336,118</u>	<u>100.00%</u>
Tax rate per \$1,000 of assessed valuation	\$ 44.30		\$ 44.20	

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 8 – CAPITAL ASSETS

Capital asset activity for the fiscal year ended June 30, 2005, was as follows:

	<u>Balance at 6/30/04</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance at 6/30/05</u>
Governmental Activities				
Nondepreciable Capital Assets				
Land	\$ 1,004,940	\$ 0	\$ 0	\$ 1,004,940
Total Nondepreciable Capital Assets	1,004,940	0	0	1,004,940
Depreciable Capital Assets				
Land Improvements	1,556,035	32,676	0	1,588,711
Buildings and Building Improvements	8,358,079	0	0	8,358,079
Furniture, Fixtures, and Equipment	3,939,856	87,486	(19,349)	4,007,993
Vehicles	1,365,466	135,161	(48,601)	1,452,026
Total Depreciable Capital Assets	<u>15,219,436</u>	<u>255,323</u>	<u>(67,950)</u>	<u>15,406,809</u>
Less Accumulated Depreciation				
Land Improvements	(434,260)	(67,505)	0	(501,765)
Buildings and Building Improvements	(3,499,582)	(146,818)	0	(3,646,400)
Furniture, Fixtures, and Equipment	(2,342,828)	(240,181)	14,537	(2,568,472)
Vehicles	(781,187)	(118,304)	44,595	(854,896)
Total Accumulated Depreciation	<u>(7,057,857)</u>	<u>(572,808)</u>	<u>59,132</u>	<u>(7,571,533)</u>
Depreciable Capital Assets, Net	<u>8,161,579</u>	<u>(317,485)</u>	<u>(8,818)</u>	<u>7,835,276</u>
Governmental Activities Capital Assets, Net	<u>\$ 9,166,519</u>	<u>\$ (317,485)</u>	<u>\$ (8,818)</u>	<u>\$ 8,840,216</u>

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 8 – CAPITAL ASSETS (continued)

Depreciation expense was charged to governmental functions as follows:

	June 30, 2005
Instruction:	
Regular	\$ 88,704
Special	8,589
Vocational	3,817
Support Services:	
Pupils	2,439
Instructional Staff	23,346
Board of Education	32
Administration	22,949
Fiscal	1,152
Operation and Maintenance of Plant	168,386
Pupil Transportation	110,127
Central	32,315
Non-Instructional Services	17,226
Extracurricular Activities	93,726
Total Depreciation Expense	\$ 572,808

NOTE 9 – INTERFUND ASSETS/LIABILITIES

At June 30, 2005, the General Fund had an interfund receivable and other governmental funds had an interfund payable, in the amount of \$65,629, resulting from short-term loans made to other governmental funds. As of June 30, 2005, the General Fund also had an Advances to Other Funds in the amount of \$68,000 representing obligations other than short-term, due to the length of time needed for repayment.

	June 30, 2005	
	<u>Interfund Receivable</u>	<u>Interfund Payable</u>
General	\$ 65,629	\$ 0
Other Governmental:		
Special Education	0	62,386
Title I	0	3,243
Total	\$ 65,629	\$ 65,629

**Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005**

NOTE 9 – INTERFUND ASSETS/LIABILITIES (continued)

	June 30, 2005	
	Advance To Other Funds	Advance From Other Funds
General	\$ 68,000	\$ 0
Other Governmental:		
Food Service	0	28,000
Athletics	0	40,000
Total	\$ 68,000	\$ 68,000

NOTE 10 – RISK MANAGEMENT

The School District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During fiscal year 2005, the School District contracted for the following insurance coverage.

Indiana Insurance Company:	
General Liability	
Per Occurrence	\$ 1,000,000
Total per Year	2,000,000
Umbrella Liability	
Per Occurrence	4,000,000
Total per Year	4,000,000
Building and contents	59,588,753
Cincinnati Insurance:	
Boiler Insurance	25,000,000
Auto Owners Insurance Company:	
Vehicle liability	1,000,000
Uninsured/Underinsured motorist	1,000,000

Settled claims have not exceeded this commercial coverage in any of the past three years, and there has been no significant reduction in insurance coverage from the prior fiscal year.

The School District participates in the Northern Buckeye Education Council Employee Insurance Benefits Program (Program), a public entity shared risk pool consisting of educational entities within Defiance, Fulton, Henry, Lucas, Williams, and Wood Counties. The School District pays monthly premiums to the Northern Buckeye Education Council for the benefits offered to its employees including medical, dental, vision, and life insurance. The Northern Buckeye Education Council is responsible for the management and operations of the Program. The agreement for the Program provides for additional assessments to all participants if the premiums are insufficient to pay the program costs for the fiscal year. Upon withdrawal from the Program, a participant is responsible for any claims not processed and paid and any related administrative costs.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 10 – RISK MANAGEMENT (continued)

The School District participates in the Northern Buckeye Education Council Workers' Compensation Group Rating Plan (Plan), an insurance purchasing pool. The Plan is intended to reduce premiums for the participants. The workers' compensation experience of the participants is calculated as one experience and a common premium rate is applied to all participants in the Plan. Each participant pays its workers' compensation premium to the State based on the rate for the Plan rather than its individual rate. Participation in the Plan is limited to entities that can meet the Plan's selection criteria. Each participant must apply annually. The Plan provides the participants with a centralized program for the processing, analysis, and management of workers' compensation claims and a risk management program to assist in developing safer work environments. Each participant must pay its premiums, enrollment or other fees, and performs its obligations in accordance with the terms of the agreement.

NOTE 11 - DEFINED BENEFIT PENSION PLANS

A. State Teachers Retirement System

The School District participates in the State Teachers Retirement System of Ohio (STRS Ohio), a cost-sharing, multiple-employer public employee retirement system. STRS Ohio provides retirement and disability benefits to members and death and survivor benefits to beneficiaries. Authority to establish and amend benefits is provided by Chapter 3307 of the Ohio Revised Code. STRS Ohio issues a stand-alone financial report that may be obtained by writing to STRS Ohio, 275 E. Broad St., Columbus, OH 43215-3371 or by calling (614) 227-4090.

New members have a choice of three retirement plans, a Defined Benefit (DB) Plan, a Defined Contribution (DC) Plan and a Combined Plan. The DB plan offers an annual retirement allowance based on final average salary times a percentage that varies based on years of service, or an allowance based on member contributions and earned interest matched by STRS Ohio funds times an actuarially determined annuity factor. The DC Plan allows members to place all their member contributions and employer contributions equal to 10.5 percent of earned compensation into an investment account. Investment decisions are made by the member. A member is eligible to receive a retirement benefit at age 50 and termination of employment. The Combined Plan offers features of both the DC Plan and the DB Plan. In the Combined Plan, member contributions are invested by the member, and employer contributions are used to fund the defined benefit payment at a reduced level from the regular DB Plan. DC and Combined Plan members will transfer to the Defined Benefit Plan during their fifth year of membership unless they permanently select the DC or Combined Plan. Existing members with less than five years of service credit as of June 30, 2001, were given the option of making a one time irrevocable decision to transfer their account balances from the existing DB Plan into the DC Plan or the Combined Plan. This option expired on December 31, 2001. Benefits are established by Chapter 3307 of the Ohio Revised Code.

A DB or Combined Plan member with five or more years credited service who becomes disabled may qualify for a disability benefit. Eligible spouses and dependents of these active members who die before retirement may qualify for survivor benefits. Members in the DC Plan who become disabled are entitled only to their account balance. If a member dies before retirement benefits begin, the member's designated beneficiary is entitled to receive the member's account balance.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 11 - DEFINED BENEFIT PENSION PLANS (continued)

For the fiscal year ended June 30, 2005, plan members were required to contribute 10 percent of their annual covered salaries. The School District was required to contribute 14 percent; 13 percent was the portion used to fund pension obligations. Contribution rates are established by the State Teachers Retirement Board, upon recommendation of its consulting actuary, not to exceed statutory maximum rates of 10 percent for members and 14 percent for employers. Chapter 3307 of the Ohio Revised Code provides statutory authority for member and employer contributions.

The School District's required contributions to the DB Plan for the fiscal years ended June 30, 2005, 2004, and 2003 were \$1,242,134, \$1,212,704, and \$1,173,614, respectively; 83 percent has been contributed for fiscal year 2005 and 100 percent for fiscal years 2004 and 2003. Contributions to the DC and Combined Plans for fiscal year 2005 were \$302 made by the School District and \$3,208 made by plan members.

B. School Employees Retirement System

The School District contributes to the School Employees Retirement System (SERS), a cost-sharing multiple employer defined benefit pension plan. SERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by Chapter 3309 of the Ohio Revised Code. SERS issues a publicly available, stand-alone financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the School Employees Retirement System, 300 East Broad Street, Suite 100, Columbus, Ohio 43215-3476 or by calling (614) 222-5853.

Plan members are required to contribute 10 percent of their annual covered salary and the School District is required to contribute at an actuarially determined rate. The current School District rate is 14 percent of annual covered payroll. A portion of the School District's contribution is used to fund pension obligations with the remainder being used to fund health care benefits; for fiscal year 2005, 10.57 percent of annual covered salary was the portion used to fund pension obligations. For fiscal year 2004, 9.09 percent of annual covered salary was the portion used to fund pension obligations. The contribution requirements of plan members and employers are established and may be amended, up to statutory maximum amounts, by the SERS Retirement Board. The School District's required contribution to SERS for the fiscal years ended June 30, 2005, 2004 and 2003 were \$240,266, \$108,432, and \$169,290, respectively; 50 percent has been contributed for fiscal year 2005 and 100 percent has been contributed for fiscal years 2004 and 2003.

C. Social Security System

Effective July 1, 1991, all employees not otherwise covered by the State Teachers Retirement System or the School Employees Retirement System have an option to choose Social Security or the State Teachers Retirement System/School Employees Retirement System. As of June 30, 2005, none of the Board of Education members have elected Social Security.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 12 – POSTEMPLOYMENT BENEFITS

A. State Teachers Retirement System

The School District provides comprehensive health care benefits to retired teachers and their dependents through the State Teachers Retirement System (STRS), and to retired non-certified employees and their dependents through the School Employees Retirement System (SERS). Benefits include hospitalization, physicians' fees, prescription drugs and reimbursement of monthly Medicare premiums. Benefit provisions and the obligations to contribute are established by the Systems based on authority granted by State statute. Both systems are funded on a pay-as-you-go basis.

STRS retirees who participated in the DB or combined plans and their dependents are eligible for health care coverage. The STRS Board has statutory authority over how much, if any, of the health care costs will be absorbed by STRS. All benefit recipients pay a portion of health care cost in the form of a monthly premium. By law, the cost of coverage paid from STRS funds is included in the employer contribution rate, currently 14 percent of covered payroll. For the fiscal year ended June 30, 2005, the STRS Board allocated employer contributions equal to 1 percent of covered payroll to the Health Care Reserve Fund. For the District, this amount \$95,549.

STRS pays health care benefits from the Health Care Stabilization Fund. At June 30, 2005, the balance in the Fund was \$3.1 billion. For the fiscal year ended June 30, 2005, net health care costs paid by STRS were \$268,739,000 and STRS had 111,853 eligible benefit recipients.

B. School Employees Retirement System

For SERS, coverage is made available to service retirees with ten or more fiscal years of qualifying service credit, and to disability and survivor benefit recipients. All retirees and beneficiaries are required to pay a portion of their premium for health care. The portion is based on years of service, Medicare eligibility, and retirement status. Premiums may be reduced for retirees whose household income falls below the poverty level.

After the allocation for basic benefits, the remainder of the employer's 14 percent contribution is allocated to providing health care benefits. For the fiscal year ended June 30, 2005, employer contributions to fund health care benefits were 3.43 percent of covered payroll, a decrease of 1.48 percent from fiscal year 2004. In addition, SERS levies a surcharge to fund health care benefits equal to 14 percent of the difference between a minimum pay and the member's pay, pro-rated for partial service credit. For fiscal year 2005, the minimum pay was established at \$27,400. However, the surcharge is capped at 2 percent of each employer's SERS salaries. The amount contributed to fund healthcare benefits, including the surcharge, amounted to \$77,967 for fiscal year 2005. The surcharge, added to the unallocated portion of the 14 percent employer contribution rate, provides for maintenance of the asset target level for the health care fund.

Healthcare benefits are financed on a pay-as-you-go basis. The target level for the health care reserve is 150 percent of projected claims less premium contributions for the next fiscal year. Expenses for health care for the fiscal year ended June 30, 2005 were \$223,444,000. As of June 30, 2005, SERS had net assets available for payment of health care benefits of \$300.8 million, which is about 111% of next year's projected net health care costs of \$335.2. SERS has approximately 62,000 participants eligible to receive benefits.

**Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005**

NOTE 13 – OTHER EMPLOYEE BENEFITS

A. Compensated Absences

The criteria for determining vacation and sick leave benefits is derived from negotiated agreements and State laws. Classified employees earn ten to twenty days of vacation per fiscal year, depending upon length of service. Unused vacation time can be carried forward with special permission and is limited to one year's accumulation. Teachers do not earn vacation time.

Teachers, administrators, and classified employees earn sick leave at a rate of one and one-fourth days per month. Sick leave may be accumulated up to a maximum of two hundred twenty days for all employees. Upon retirement, payment is made for one-fourth of accrued, but unused sick leave credit to a maximum of fifty-five days for all employees.

B. Health Care Benefits

The School District provides medical, dental, vision, and life insurance to most employees through the Northern Buckeye Education Council Employee Insurance Benefits Program.

NOTE 14 – LONG-TERM OBLIGATIONS

Changes in the School District's long-term obligations during fiscal year 2005 were as follows:

	Interest Rate	Balance At 6/30/04	Additions	Reductions	Balance at 6/30/05	Amounts due within one year
Energy Conservation Loan	2.65%	\$ 446,250	\$ 0	\$ 148,750	\$ 297,500	\$ 148,750
Compensated absences payable		1,189,276	180,064	71,812	1,297,528	54,355
Capital Leases payable		<u>44,556</u>	<u>0</u>	<u>13,855</u>	<u>30,701</u>	<u>14,829</u>
Total Governmental Activities long-term obligations		<u>\$ 1,680,082</u>	<u>\$ 180,064</u>	<u>\$ 234,417</u>	<u>\$ 1,625,729</u>	<u>\$ 217,934</u>

Energy Conservation Loan - On February 18, 2003, the School District obtained energy conservation loan with an interest rate of 2.65 percent. Principal installments are payable February 1 and August 1 in the years 2003 through 2007. The loan will mature February 1, 2007. The loan is being retired from the Bond Retirement debt service fund.

Compensated absences will be paid from the General Fund and from the Food Service special revenue fund. Capital leases will be paid from the General Fund.

The School District's overall debt margin was \$21,540,251 with an unvoted debt margin of \$239,336 at June 30, 2005.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 14 – LONG-TERM OBLIGATIONS (continued)

Principal and interest requirements to retire energy conservation loan outstanding at June 30, 2005, were as follows.

<u>Fiscal Year</u> <u>Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2006	\$ 148,750	\$ 6,898	\$ 155,648
2007	<u>148,750</u>	<u>2,957</u>	<u>151,707</u>
	<u>\$ 297,500</u>	<u>\$ 9,855</u>	<u>\$ 307,355</u>

NOTE 15 – CAPITAL LEASES- LESSEE DISCLOSURE

The School District has entered into a capitalized lease for equipment. The lease meets the criteria of a capital lease as defined by Statement of Financial Accounting Standards No. 13, "Accounting for Leases", which defines a capital lease generally as one which transfers benefits and risks of ownership to the lessee. Capital lease payments are reflected as debt service expenditures on the statement of revenues, expenditures, and changes in fund balances for the governmental funds. Principal payments in 2005 were \$13,855.

	<u>Governmental</u> <u>Activities</u>
Property under Capital Lease	\$ 69,595
Less Accumulated Depreciation	<u>(40,600)</u>
Total June 30, 2005	<u>\$ 28,995</u>

The following is a schedule of the future long-term minimum lease payments required under the capital lease and the present value of the minimum lease payments as of June 30, 2005.

<u>Fiscal Year</u> <u>Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2006	\$ 14,829	\$ 1,635	\$ 16,464
2007	<u>15,872</u>	<u>592</u>	<u>16,464</u>
	<u>\$ 30,701</u>	<u>\$ 2,227</u>	<u>\$ 32,928</u>

NOTE 16 – SET-ASIDES

The School District is required by State statute to annually set aside, in the General Fund, an amount based on a statutory formula for the purchase of textbooks and other instructional materials, and an equal amount for the acquisition and construction of capital improvements. Amounts not spent by the end of the fiscal year or offset by similarly restricted resources received during the fiscal year must be held in cash at fiscal year end. These amounts must be carried forward and used for the same purposes in future years.

**Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005**

NOTE 16 – SET-ASIDES (continued)

The following cash basis information identifies the changes in the fund balance reserves for textbooks and capital improvements during fiscal year 2005.

	Textbooks	Capital Improvements
Balance June 30, 2004	\$ 0	\$ 504,242
Current Year Set Aside Requirement	339,888	339,888
Qualifying Expenditures	(489,645)	(298,057)
Excess Qualifying Expenditures from FY04	(708,958)	0
Balance June 30, 2005	(858,715)	546,073
Amount Carried Forward to Fiscal Year 2006	\$ 0	\$ 546,073

The School District had qualifying expenditures during the fiscal year that reduced the textbooks set aside amount below zero. This amount may be used to reduce the set aside requirement in future fiscal years.

NOTE 17 – INTERFUND TRANSFERS

During fiscal year 2005, the General Fund made transfers to other governmental funds, in the amount of \$159,754, to move receipts to the debt service fund as debt payments came due.

NOTE 18 – JOINTLY GOVERNED ORGANIZATIONS

A. Northwest Ohio Computer Association

The School District is a participant in the Northwest Ohio Computer Association (NWOCA), which is a computer consortium. NWOCA is an association of educational entities within the boundaries of Defiance, Fulton, Henry, Lucas, Williams, and Wood Counties. The organization was formed for the purpose of applying modern technology with the aid of computers and other electronic equipment to administrative and instructional functions among member educational entities.

The NWOCA Assembly consists of the superintendent from each participating educational entity and a representative from the fiscal agent. The Assembly elects the governing council of two representatives from each of the six counties in which member educational entities are located and the representative from the member educational entity serving as fiscal agent for NWOCA. The degree of control exercised by any participating educational entity is limited to its representation on the Governing Council. During fiscal year 2005, the School District paid \$85,974 to NWOCA for various services. Financial information can be obtained from Cindy Siler, who serves as Treasurer, 22-900 State Route 34, Archbold, Ohio 43502.

**Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005**

NOTE 18 – JOINTLY GOVERNED ORGANIZATIONS (continued)

B. Northern Buckeye Education Council

The Northern Buckeye Education Council (NBEC) was established in 1979 to foster cooperation among educational entities located in Defiance, Fulton, Henry, Lucas, Williams, and Wood Counties. NBEC is organized under Ohio laws as a regional council of governments pursuant to a written agreement entered into by its member educational entities and bylaws adopted by the representatives of the member educational entities. NBEC is governed by an elected board consisting of two representatives from each of the six counties in which the member educational entities are located. The Board is elected from an assembly consisting of a representative from each participating educational entity. Financial information can be obtained from the Northern Buckeye Education Council, Cindy Siler, who serves as Treasurer, 22-900 State Route 34, Archbold, Ohio 43502.

C. Four County Career Center

The Four County Career Center (Career Center) is a distinct political subdivision of the State of Ohio which provides vocational education to students. The Career Center is operated under the direction of a board consisting of five representatives from the Northwest Ohio Educational Service Center and one representative from the participating school districts elected boards. The Career Center possesses its own budgeting and taxing authority. The degree of control exercised by the School District is limited to its representation on the Board. Financial information can be obtained from the Four County Career Center, Lois Knuth, who serves as Treasurer, Route 1, Box 245A, Archbold, Ohio 43502.

D. Northwestern Ohio Educational Research Council, Inc.

The Northwestern Ohio Educational Research Council, Inc. (NOERC) is a jointly governed organization formed to bring educational entities into a better understanding of their common educational problems, facilitate and conduct practical educational research, coordinate educational research among members, provide a means for evaluating and disseminating the results of research, serve as a repository for research and legislative materials, and provide opportunities for training. The NOERC serves a twenty-five county area in Northwest Ohio. The Board of Directors consists of superintendents from two educational service centers, two exempted village school districts, five local school districts, and five city school districts, as well as representatives from two private or parochial schools and three institutions of higher education. Each active member is entitled to one vote on all issues addressed by the Board of Directors. Financial information can be obtained from the Northwestern Ohio Educational Research Council, Inc., Box 456, Ashland, Ohio 44805.

E. Northwest Ohio Special Education Regional Resource Center

The Northwest Ohio Special Education Regional Resource Center (SERRC) is a jointly governed organization formed to provide services to families, educators, and agencies regarding educational law and curriculum and instruction for students with disabilities. The SERRC serves a thirteen county area in Northwest Ohio. The Governing Board consists of superintendents from each of the cooperating School Districts, the fiscal agent superintendent, two parents of children with disabilities, one superintendent of a county board of MR/DD, one representative from a chartered non-public school, one representative from the University of Toledo, one representative from Bowling Green State University, one representative from a community school, and any other representatives from other agencies as designated by the Governing Board or the Ohio Department of

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 18 – JOINTLY GOVERNED ORGANIZATIONS (continued)

Education. The degree of control exercised by any participating school district is limited to its representation on the Board. Financial information can be obtained from Dave Michel, Eastwood Local School District, 4800 Sugar Ridge Road, Pemberville, Ohio 43450.

F. Northwest Ohio Regional Professional Development Center

The Northwest Ohio Regional Professional Development Center (RPDC) is a jointly governed organization among the school districts in Defiance, Erie, Fulton, Henry, Lucas, Ottawa, Sandusky, Williams, and Wood counties. The RPDC focuses on the implementation of academic content standards and the deployment of State initiatives. All activities reflect definition of high quality professional development, including job-embedded, connected to strategic goals, sustained, intensive skill building, and measurement of impact on student learning.

The Center is governed by a fifteen member board made up of representatives from the participating school districts, the business community, and two institutions of higher learning. The degree of control exercised by any participating school district is limited to its representation on the Board. Financial information can be obtained from the Northwest Ohio Regional Professional Development Center, 414 Emerald Street, 2nd Floor, Toledo, Ohio 43602.

NOTE 19 – INSURANCE POOLS

A. Northern Buckeye Education Council Employee Insurance Benefits Program

The Northern Buckeye Education Council Employee Insurance Benefits Program (Program) is a public entity shared risk pool consisting of educational entities within Defiance, Fulton, Henry, Lucas, Williams, and Wood Counties. The Program is governed by the Northern Buckeye Education Council (NBEC) and its participating members.

B. Northern Buckeye Education Council Workers' Compensation Group Rating Plan

The School District participates in a group rating plan for workers' compensation as established under Section 4123.29 of the Ohio Revised Code. The Northern Buckeye Education Council Workers' Compensation Group Rating Plan (Plan) was established through the Northern Buckeye Education Council (NBEC) as an insurance purchasing pool. The Plan is governed by the Northern Buckeye Education Council and the participants of the Plan. The Executive Director of the NBEC coordinates the management and administration of the Plan. Each year, the participants pay an enrollment fee to the Plan to cover the costs of administering the program.

Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005

NOTE 20 – STATE SCHOOL FUNDING DECISION

On December 11, 2002, the Ohio Supreme Court issued its latest opinion regarding the State’s school funding plan. The decision reaffirmed earlier decisions that Ohio’s current school funding plan is unconstitutional.

The Supreme Court relinquished jurisdiction over the case and directed “...the Ohio General Assembly to enact a school funding scheme that is thorough and efficient...”. The School District is currently unable to determine what effect, if any, this decision will have on its future State funding and its financial operations.

NOTE 21 - CONTINGENCIES

A. Grants

The School District received financial assistance from federal and state agencies in the form of grants. The expenditure of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and is subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the General Fund or other applicable funds. However, in the opinion of management, any such disallowed claims will not have a material adverse effect on the overall financial position of the School District at June 30, 2005.

B. Litigation

There are currently no matters in litigation with the School District as defendant.

NOTE 22 – RESTATEMENT OF PRIOR YEAR FUND BALANCES/NET ASSETS

Change in Accounting Principles

For fiscal year 2005, the District has implemented GASB Statement No. 40, “Deposit and Investment Risk Disclosures” and GASB Technical Bulletin 2004-2, “Recognition of Pension and Other Postemployment Benefit Expenditures/Expenses and Liabilities by Cost-Sharing Employers”.

GASB Statement No. 40 establishes and modifies disclosure requirements related to investment risks: credit risk (including custodial credit risk and concentrations of credit risk) and interest rate risk. This statement also establishes and modifies disclosure requirements for custodial credit risk on deposits.

GASB Technical Bulletin No. 2004-2 addresses the amount that should be recognized as expenditure/expense and as a liability each period by employers participating in a cost-sharing multiple-employer pension and other postemployment benefit (OPEB) plans.

The implementation of GASB Statement No. 40 did not have an effect on the financial statements of the District, however additional note disclosure can be found in Note 4. The implementation of GASB Technical Bulletin No. 2004-2 had the following effect on the fund balances of the major and non-major funds of the District as they were previously reported as of June 30, 2004:

**Defiance City School District
Defiance County
Notes to the Basic Financial Statements
For the year ending June 30, 2005**

NOTE 22 – RESTATEMENT OF PRIOR YEAR FUND BALANCES/NET ASSETS (continued)

	<u>General</u>	Nonmajor <u>Gov't Funds</u>	<u>Total</u>
Fund Balances, June 30, 2004	\$ 1,793,305	\$ 815,173	\$2,608,478
GASB Technical Bulletin No. 2004-2	<u>(204,070)</u>	<u>(89,769)</u>	<u>(293,839)</u>
Restated Fund Balances, July 1, 2004	<u>\$ 1,589,235</u>	<u>\$ 725,404</u>	<u>\$2,314,639</u>

We also noted an incorrect balance in the prior year ending budgetary fund balance in the General Fund. The beginning General Fund budgetary fund balance required an increase of \$539,278, to \$2,459,612.

DEFIANCE CITY SCHOOL DISTRICT
Schedule of Federal Awards Expenditures
For The Fiscal Year Ended June 30, 2005

Federal Grantor/Pass Trough Grantor Program Title	Project #	Federal CFDA #	Receipts	Disbursements
U. S. DEPARTMENT OF AGRICULTURE				
Passed Through Ohio Department Of Education				
Nutrition Cluster:				
Federal Donated Commodities	-	10.550	\$ 70,789	\$ 70,789
National School Lunch Program	043869-LL-P4	10.555	250,150	250,150
Special Milk Program For Children	043869-LL-P4	10.556	1,869	1,869
School Breakfast Program	043869-05-PU	10.553	<u>39,925</u>	<u>39,925</u>
Total Department Of Agriculture & Nutrition Cluster			362,733	362,733
U. S. DEPARTMENT OF HEALTH & HUMAN SERVICES				
Passed Through Ohio Department Of Mental Retardation & Developmental Disabilities				
Medical Assistance Plan (Medicaid: Title XIX)	N/A	93.778	\$ 46,935	\$ 46,935
Total Department Of Health & Human Services			46,935	46,935
U. S. DEPARTMENT OF EDUCATION				
Passed Through Ohio Department Of Education				
Special Education Cluster:				
Special Education (Part B-IDEA)	043869-6B-SF	84.027	\$ 439,280	\$ 439,280
Total Special Education Cluster			<u>439,280</u>	<u>439,280</u>
Grants To Local Educational Agencies (ESEA Title I)	043869-CI-SI	84.010	\$ 310,812	\$ 310,812
Innovative Educational Program Strategies (Title V)	043869-C2-S1	84.298	14,254	14,254
Title II-D Educational Technology	043869-TJ-S1	84.318	2,927	2,927
Improving Teacher Quality (Title II-A)	043869-TR-S1	84.367	128,192	128,192
Safe & Drug-Free Schools (Title IV-A)	043869-DR-S1	84.186	<u>9,124</u>	<u>9,124</u>
Total Department Of Education			<u>904,589</u>	<u>904,589</u>
TOTAL FEDERAL ASSISTANCE			<u><u>\$ 1,314,257</u></u>	<u><u>\$ 1,314,257</u></u>

**Defiance City School District
Defiance County, Ohio
Notes to the Schedule of Federal Awards Expenditures
For the Year Ended June 30, 2005**

1. Significant Accounting Policies

The accompanying schedule of federal awards expenditures is a summary of the activity of the Defiance City School District's federal award programs. The schedule has been prepared on the cash basis of accounting. Consequently, certain revenues are recognized when received rather than when earned, and certain expenditures are recognized when paid rather than when the obligation is incurred.

2. Food Distribution

Nonmonetary assistance is reported in the schedule at fair market value of the commodities received and disbursed. Monies are commingled with State grants. It is assumed federal monies are expended first. At June 30, 2005, the District had immaterial food commodities in inventory recorded in the Food Service Fund.

INDEPENDENT ACCOUNTANT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF STATEMENTS REQUIRED BY GOVERNMENT AUDITING STANDARDS

Board of Education
Defiance City School District
629 Arabella St
Defiance, OH 43512

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Defiance City School District as of and for the year ended June 30, 2005, which collectively comprise the District's basic financial statements and have issued our report thereon dated February 24, 2006, wherein we noted the District implemented GASB Technical Bulletin No. 2004-2 and GASB Statement No. 40. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Controls Over Financial Reporting

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control over financial reporting. Our consideration of internal control would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the District's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. A reportable condition is described in the accompanying Schedule of Findings and Questioned Costs as item 2005-1.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level of risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration on the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider the reportable condition described above to be a material weakness.

We also noted certain additional internal control matters that we reported to management of the District in a separate letter dated February 24, 2006.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants agreements and other matters, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

However, we noted certain immaterial instances of noncompliance that we reported to management of the District in a separate letter dated February 24, 2006.

This report is intended for the information and use of management, the Board of Trustees, federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Charles E. Harris & Associates, Inc.
February 24, 2006

Charles E. Harris & Associates, Inc.
Certified Public Accountants

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Cleveland OH 44113-1306
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**REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO
EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE
IN ACCORDANCE WITH OMB CIRCULAR A-133**

Board of Education
Defiance City School District
629 Arabella St
Defiance, OH 43512

Compliance

We have audited the compliance of the Defiance City School District with the types of compliance requirements described in *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its major federal program for the year ended June 30, 2005. The District's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of the District's management. Our responsibility is to express an opinion on the District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the District's compliance with those requirements.

In our opinion, the District complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended June 30, 2005.

Internal Control Over Compliance

The management of the District is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the District's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with *OMB Circular A-133*.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

This report intended for the information and use of management, the Board of Trustees, federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Charles E. Harris & Associates, Inc.
February 24, 2006

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
OMB CIRCULAR A-133 SECTION .505**

**Defiance City School District
Defiance County
June 30, 2005**

1. SUMMARY OF AUDITOR'S RESULTS

(d)(1)(i)	<i>Type of Financial Statement Opinion</i>	Unqualified
(d)(1)(ii)	<i>Were there any other reportable control weakness conditions reported at the financial statement level (GAGAS)?</i>	Yes
(d)(1)(iii)	<i>Was there any reported material non-compliance at the financial statement level (GAGAS)?</i>	No
(d)(1)(iv)	<i>Were there any material internal control weakness conditions reported for major federal programs?</i>	No
(d)(1)(iv)	<i>Were there any other reportable internal control weakness conditions reported for major federal programs?</i>	No
(d)(1)(v)	<i>Type of Major Programs' Compliance Opinion</i>	Unqualified
(d)(1)(vi)	<i>Are there any reportable findings under Section .510</i>	No
(d)(1)(vii)	<i>Major Programs:</i>	Nutrition Cluster: Federal Donated Commodities CFDA#10.550 National School Lunch Program CFDA#10.555 Special Milk Program For Children CFDA#10.556 School Breakfast Program CFDA#10.553
(d)(1)(viii)	<i>Dollar Threshold: Type A\B Programs</i>	Type A: > \$300,000 Type B: all others
(d)(1)(ix)	<i>Low Risk Auditee?</i>	Yes

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS
OMB CIRCULAR A-133 SECTION .505 (Continued)**

**DEFIANCE CITY SCHOOL DISTRICT
DEFIANCE COUNTY
June 30,2005**

**2. FINDINGS RELATED TO THE FINANCIAL STATEMENTS REQUIRED TO BE REPORTED
IN ACCORDANCE WITH GAGAS**

Finding 2005-1 Reportable Condition

During the course of our audit, we noted that adequate updated records for property and equipment items are not being maintained on a school wide basis. We determined that several items purchased in prior years were incorrectly included in current year additions. The carrying amount for vehicles was not reconciled to the fixed asset reports and the depreciation for furniture, fixture, equipment and vehicles were not reconciled to depreciation reports. The effects of these conditions were that net fixed assets and depreciation was overstated.

In addition, the District has not performed a fixed asset valuation for many years. Performing a valuation for fixed assets aids in determining the physical presence of assets recorded in the District's records, in accounting for property disposals, substantiating insurance claims for lost or damaged items, and in providing controls to safeguard the assets. It is recommended that the District perform a valuation for fixed assets and properly update the physical inventory and depreciation records annually to ensure assets are added and deleted as required.

3. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS

None.

**DEFIANCE CITY SCHOOL DISTRICT
DEFIANCE COUNTY**

Schedule of Prior Audit Findings
June 30, 2005

FINDING NUMBER	FUNDING SUMMARY	FULLY CORRECTED?	Not Corrected. Partially Corrected; Significantly Different Corrective Action Taken; or Finding No Longer Valid; Explain
2004-1	The School District did not properly update the physical inventory and depreciation records annually to ensure assets are added and deleted as required	No	Not Corrected. Reissued as Finding 2005-1.
2004-2	Lack of adequate supporting documentation for travel reimbursements (ORC 102.03(D) and (E), 2921.42(A) and 2921.43(A)).	Yes	Adequate supporting documentation in place. Finding no longer valid.
2004-3	The school did not keep mileage logs or personal usage reports on any school vehicles (ORC 3313.172).	Yes	Fully Corrected. Finding no longer valid.
2004-4	Public funds were not deposited in a timely manner (ORC 9.38).	Yes	Fully Corrected. Finding no longer valid.
2004-5	Expenditures exceeded appropriation at the legal level of control (ORC 5705.41(B)).	Yes	Fully Corrected. Finding no longer valid.
2004-6	No amended certificate of available resources obtained when a deficiency of revenue reduces available resources below the current level of appropriation (ORC 5705.36).	No	Partially corrected. Finding reissued in management letter.

**DEFIANCE CITY SCHOOL DISTRICT
DEFIANCE COUNTY**

Schedule of Prior Audit Findings
June 30, 2005

2004-7	The total appropriations from several funds exceeded the total of the estimated resources (ORC 5705.39).	No	Partially Corrected. Finding reissued in management letter.
2004-8	Lack of proper warrant drawn against an appropriate fund (ORC 5705.41(C)).	Yes	Fully Corrected. Finding no longer valid.
2004-9	Lack of proper certification and encumbrance of funds prior to the expenditure (ORC 5705.41).	No	Partially Corrected. Finding reissued in management letter.
2004-10	Failure to publish a notice in the local newspaper for public inspection of annual reports (ORC 117.38).	No	Not Corrected. Finding reissued in management letter.



**Auditor of State
Betty Montgomery**

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DEFIANCE CITY SCHOOL DISTRICT

DEFIANCE COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

**CERTIFIED
MAY 4, 2006**