

**MEASURE A – STRONG SCHOOLS BOND OF
PALO ALTO UNIFIED SCHOOL DISTRICT**

**AUDIT REPORT
FOR THE FISCAL YEAR ENDED
JUNE 30, 2013**

San Diego

Los Angeles

**San Francisco
Bay Area**

christywhite
A PROFESSIONAL
ACCOUNTANCY CORPORATION *associates*

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
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For the Fiscal Year Ended June 30, 2013**

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**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Introduction and Citizens’ Oversight Committee Member Listing
June 30, 2013**

The Palo Alto Unified School District (the “District”) was founded on March 20, 1893 under the laws of the State of California. This District operates under a locally elected five-member Board form of government and provides educational services to grades K – 12 as mandated by the state and federal agencies. The District operates twelve elementary, three middle, two high schools, an adult education program, a Young Fives program and two children’s centers.

In June 2008, the voters of the Palo Alto Unified School District approved by more than the required 55% favorable vote the Measure A – Strong Schools Bond (“Measure A”), authorizing the issuance and sale of general obligation bonds, not to exceed \$378,000,000. The Measure A – Strong Schools Bond is a Proposition 39 bond. The passage of Proposition 39 in November 2000 amended the California Constitution to include accountability provisions. Specifically, the District must conduct an annual independent performance audit to ensure that funds have been expended only on the specific projects listed in the full text of the Measure A – Strong Schools Bond ballot measure as well as an annual, independent financial audit of the proceeds from the sale of the bonds until all of the proceeds have been expended for bond-designated facilities projects.

Measure A bonds were issued by the District, through the County of Santa Clara. On August 27, 2008, Series 2008 of the Measure A bond authorization was issued, which consisted of current interest and capital appreciation bonds with an initial par amount of \$119,999,249 with stated interest rates of 2.50% to 5.50% and maturing through August 1, 2033. On July 13, 2010, Series 2010 of the Measure A bond authorization was issued and was designated as qualified school construction bonds under Section 54F of the Internal Revenue Code of 1986. These bonds provide a federal subsidy to the District which significantly decreases overall interest cost. The bonds were issued with initial par amount of \$25,000,000, with stated interest rates of 4.662% to 5.862% and maturing through July 1, 2027. The net interest rate of the issuance is 0.40% after accounting for the federal subsidy. On March 5, 2013, Series 2013 of the Measure A bond authorization was issued, which consisted of current interest bonds with an initial par amount of \$70,000,000 with stated interest rates of 2.00% to 3.50% and maturing through July 1, 2036. For Measure A, the District has elected to conform to the requirements of low bid construction delivery, as opposed to an alternate model such as lease-leaseback. In doing so, the District has likely increased the degree of the program’s cost accountability.

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT**

Introduction and Citizens’ Oversight Committee Member Listing, continued

June 30, 2013

Upon passage of Proposition 39, an accompanying piece of legislation, AB 1908 (Chapter 44, Statutes of 2000), was also enacted, which amended the Education Code to establish additional procedures which must be followed if a District seeks approval of a bond measure pursuant to the 55% majority authorized in Measure A including formation, composition and purpose of the Citizens’ Oversight Committee, and authorization for injunctive relief against the improper expenditure of bond revenues.

The Citizens’ Oversight Committee was comprised of the following members as of June 30, 2013:

<u>Name</u>	<u>Title</u>	<u>Representation</u>
Todd Collins	Chair	PTA & Taxpayers Organization
Helene Leichter	Vice Chair	Parent
Arienne Teherani	Member	Parent
Bruce Whitson	Member	Parent
Walt Hays	Member	Senior Citizens’ Organization
Catherine Garber	Member	Business Organization
James Cowie	Member	Business Organization & Parent

INDEPENDENT AUDITORS' REPORT

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John Dominguez, CPA, CFE

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State Board of Accountancy

Governing Board Members and
Measure A Citizens' Oversight Committee
Palo Alto Unified School District
Palo Alto, California

Report on the Financial Statements

We have audited the accompanying financial statements of the Measure A – Strong Schools Bond of Palo Alto Unified School District (the "District") as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Measure A - Strong Schools Bond's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express 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 financial statements are free from material misstatement.

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

Auditor's Responsibility (continued)

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

As discussed in Note 1A, the financial statements present only the individual Proposition 39 Bond Building Fund, consisting of the net construction proceeds of the Measure A – Strong Schools Bond general obligation bonds as issued by the District, through the County of Santa Clara, and are not intended to present fairly the financial position of the District in conformity with generally accepted accounting principles.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Measure A – Strong Schools Bond of Palo Alto Unified School District as of June 30, 2013 and the respective changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 22, 2013 on our consideration of the Measure A – Strong Schools Bond's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Measure A - Strong Schools Bond's internal control over financial reporting and compliance.

Report on Other Legal and Regulatory Requirements

In accordance with the requirements of Proposition 39, as incorporated in California Constitution Article 13A, we have also issued our performance audit report dated September 22, 2013 on our consideration of the Measure A – Strong Schools Bond's compliance with the requirements of Proposition 39. That report is an integral part of our audit of the Measure A – Strong Schools Bond for the fiscal year ended June 30, 2013 should be considered in assessing the results of our financial audit.



San Diego, California
September 22, 2013

FINANCIAL SECTION

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Balance Sheet
June 30, 2013**

ASSETS	
Cash in county treasury	\$ 68,555,771
Cash collections awaiting deposit	1,924
Accounts receivable	70,587
Due from other funds	<u>14,768</u>
Total Assets	\$ <u>68,643,050</u>
LIABILITIES AND FUND BALANCE	
Liabilities	
Accounts payable	<u>\$ 8,932,730</u>
Total Liabilities	<u>8,932,730</u>
Fund Balance	
Restricted for capital projects	<u>59,710,320</u>
Total Liabilities and Fund Balance	\$ <u>68,643,050</u>

The accompanying notes to financial statements are an integral part of this statement.

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Statement of Revenues, Expenditures and Changes in Fund Balance
For the Fiscal Year Ended June 30, 2013**

REVENUES	
Interest income	\$ 238,627
Total Revenues	<u>238,627</u>
EXPENDITURES	
Facilities acquisition and construction	65,574,246
Total Expenditures	<u>65,574,246</u>
Excess (Deficiency) of Revenues Over (Under) Expenditures	<u>(65,335,619)</u>
OTHER FINANCING SOURCES	
Interfund transfer-in	2,720,829
Proceeds from long-term debt	70,000,000
Total Other Financing Sources	<u>72,720,829</u>
Net Change in Fund Balance	7,385,210
Fund Balance, July 1, 2012	<u>52,325,110</u>
Fund Balance, June 30, 2013	<u>\$ 59,710,320</u>

The accompanying notes to financial statements are an integral part of this statement.

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements
June 30, 2013**

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The Palo Alto Unified School District (the “District”) was founded on March 20, 1893 under the laws of the state of California. This District operates under a locally elected five-member Board form of government and provides educational services to grades K – 12 as mandated by the state and federal agencies. The District operates twelve elementary, three middle, two high schools, an adult education program, a Young Fives program and two children’s centers.

On June 3, 2008 the District voters authorized \$378 million in general obligation bonds (“Measure A”) to provide safe and modern schools; accommodate enrollment growth; upgrade aging classrooms, libraries, computer and science labs; repair or replace roofs, plumbing, heating, ventilation and electrical systems; improve fire alarms and school security; meet current earthquake standards; provide current technology; and replace old portables with permanent classrooms.

An advisory committee to the District’s Governing Board and Superintendent, the Measure A Citizens’ Oversight Committee (“COC”) was established pursuant to the requirements of state law and the provisions of Measure A. The purpose of the COC is to inform the public concerning the use of bond proceeds. The COC is required by state law to actively review and report on the proper expenditure of taxpayers’ money for school construction. The COC provides oversight and advises the public as to whether the District is spending the Measure A – Strong Schools Bond funds for school capital improvements within the scope of projects outlined in the Measure A – Strong Schools Bond Project List. In fulfilling its duties, the COC reviews, among other things, the District’s annual performance and financial audits of Measure A activity.

The statements presented are for the individual Measure A – Strong Schools Bond of the District, consisting of the net construction proceeds of Measure A Series 2008, Series 2010, and Series 2013 general obligation bonds as issued by the District, through the County of Santa Clara, and are not intended to be a complete presentation of the District’s financial position or results of operations.

B. Accounting Policies

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

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements, continued
June 30, 2013**

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES (continued)

C. Basis of Accounting

Basis of accounting refers to when revenues and expenditures are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of measurement made, regardless of the measurement focus applied.

The financial statements are presented on the modified accrual basis of accounting. Under the modified accrual basis of accounting, revenues are recorded when susceptible to accrual; i.e., both measurable and 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. Expenditures are generally recognized under the modified accrual basis of accounting when the related liability is incurred.

D. Encumbrances

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

E. Deposits and Investments

In accordance with Education Code Sections 15357 and 41001, the District maintains a portion of its cash in the Santa Clara County Treasury. The county pools these funds with those of other districts in the county and invests the cash. These pooled funds are carried at cost, which approximates market value. Interest earned is deposited quarterly into participating funds. Any investment losses are proportionately shared by all funds in the pool.

F. Use of Estimates

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

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements, continued
June 30, 2013**

NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES (continued)

G. Budgets and Budgetary Accounting

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

These budgets are revised by the District's Governing Board during the year to give consideration to unanticipated income and expenditures. Formal budgetary integration was employed as a management control device during the year for all budgeted funds. The District employs budget control by minor object and by individual appropriation accounts. Expenditures cannot legally exceed appropriations by major object account.

H. Fund Balance

Under GASB Statement No. 54, fund balance is divided into five classifications based primarily on the extent to which the District is bound to observe constraints imposed upon the use of the resources in the governmental funds. The fund balance in Measure A – Strong Schools Bond fund is considered restricted.

The restricted fund balance classification reflects amounts subject to externally imposed and legally enforceable constraints. Such constraints may be imposed by creditors, grantors, contributors, or laws or regulations of other governments, or may be imposed by law through constitutional provisions or enabling legislation.

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements, continued
June 30, 2013**

NOTE 2 – CASH AND INVESTMENTS

Summary of Cash and Investments

Cash and investments as of June 30, 2013 consist of the following:

Cash in county treasury	\$	68,555,771
Cash collections awaiting deposit		1,924
Total cash and investments	\$	<u>68,557,695</u>

Policies and Practices

The District is authorized under California Government Code to make direct investments in local agency bonds, notes, or warrants within the State; U.S. Treasury instruments; registered State warrants or treasury notes; securities of the U.S. Government, or its agencies; bankers acceptances; commercial paper; certificates of deposit placed with commercial banks and/or savings and loan companies; repurchase or reverse repurchase agreements; medium term corporate notes; shares of beneficial interest issued by diversified management companies, certificates of participation, obligations with first priority security; and collateralized mortgage obligations. Investments of debt proceeds held by trustees are governed by the provisions of debt agreements rather than the general provisions of the California Government Code. These provisions allow for the acquisition of investment agreements with maturities up to 30 years.

Cash in County Treasury – The District is considered to be an involuntary participant in an external investment pool as the District is required to deposit all receipts and collections of monies with their County Treasurer (Education Code Section 41001). The fair value of the District’s investment in the pool is reported in the accounting financial statements at amounts based upon the District’s pro-rata share of the fair value provided by the County Treasurer for the entire portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by the County Treasurer, which is recorded on the amortized cost basis.

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements, continued
June 30, 2013**

NOTE 2 – CASH AND INVESTMENTS (continued)

General Authorizations

Except for investments by trustees of debt proceeds, the authority to invest District funds deposited with the county treasury is delegated to the County Treasurer and Tax Collector. The table below identifies examples of the investment types permitted in the investment policy:

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

Limitations as they relate to interest rate risk, credit risk, and concentration of credit risk are described below:

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The District manages its exposure to interest rate risk by investing in the County Treasury. The District maintains an investment with the Santa Clara County Investment Pool with a fair value of approximately \$68,614,043 and an amortized book value of \$68,555,771. The weighted average maturity for this pool as of June 30, 2013 is 374 days.

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements, continued
June 30, 2013**

NOTE 2 – CASH AND INVESTMENTS (continued)

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Per County investment policy, the investments within the Santa Clara County Investment Pool are rated A or higher by Moody's Investors Service.

Concentration of Credit Risk

The investment policy of the District contains no limitations on the amount that can be invested in any one issuer beyond the amount stipulated by the California Government Code. District investments that are greater than 5 percent of total investments are in either an external investment pool or mutual funds and are therefore exempt.

NOTE 3 – ACCOUNTS RECEIVABLE

Accounts receivable of \$70,587 as of June 30, 2013 consisted of interest earned on the District's investment in the County Treasury.

NOTE 4 – INTERFUND TRANSACTIONS

Interfund Receivables/Payables (Due From/Due To)

The individual interfund receivable consisted of \$14,768 due from the General Fund to reimburse the Building Fund for funds that were deposited into the incorrect fund.

Transfers

The individual interfund transfer consisted of \$2,720,829 transferred from the County School Facilities Fund related to a state funds transfer for Palo Alto High School's Media Arts Project.

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements, continued
June 30, 2013**

NOTE 5 – CONSTRUCTION COMMITMENTS

The Measure A - Strong Schools Bond had construction commitments of \$20,478,435 as of June 30, 2013.

NOTE 6 – MEASURE A – STRONG SCHOOLS BOND GENERAL OBLIGATION BONDS

As of June 30, 2013, the principal balance outstanding on the District's Measure A – Strong Schools Bond ("Measure A") general obligation bonds, including accreted interest to date, was \$237,491,156.

- On August 27, 2008, Series 2008 bonds of the Measure A bond authorization were issued, which consisted of current interest and capital appreciation bonds with an initial par amount of \$119,999,249 with stated interest rates of 2.50% to 5.50% and maturing through August 1, 2033.
- On July 13, 2010, Series 2010 of the Measure A bond authorization was issued and was designated as qualified school construction bonds under Section 54F of the Internal Revenue Code of 1986. The bonds were issued with initial par amount of \$25,000,000, with stated interest rates of 4.662% to 5.862% and maturing through July 1, 2027.
- On March 5, 2013, Series 2013 of the Measure A bond authorization was issued, which consisted of current interest bonds with an initial par amount of \$70,000,000 with stated interest rates of 2.00% to 3.50% and maturing through July 1, 2036.

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements, continued
June 30, 2013**

NOTE 6 – MEASURE A – STRONG SCHOOLS BOND GENERAL OBLIGATION BONDS (continued)

Series 2008 General Obligation Bond

As of June 30, 2013, the principal balance outstanding on the Measure A Series 2008 general obligation bonds, including accreted interest to date, was \$142,491,156. The annual requirements to amortize Measure A Series 2008 general obligation bonds payable outstanding as of June 30, 2013, are as follows:

Fiscal Year Ended June 30,	Principal (including accreted interest to date)	Accreted Interest	Current Interest to Maturity	Total
2014	\$ 2,350,000	\$ -	\$ 148,775	\$ 2,498,775
2015	2,805,000	-	84,150	2,889,150
2016	3,155,345	414,656	-	3,570,001
2017	3,461,785	653,215	-	4,115,000
2018	3,903,510	971,490	-	4,875,000
2019-2023	28,695,572	14,209,429	-	42,905,001
2024-2028	49,024,354	44,050,647	-	93,075,001
2029-2033	41,919,530	65,580,470	-	107,500,000
2034	7,176,060	14,648,940	-	21,825,000
Total	\$ 142,491,156	\$ 140,528,847	\$ 232,925	\$ 283,252,928

Series 2010 Qualified School Construction Bonds

As of June 30, 2013, the principal balance outstanding on the Measure A Series 2010 qualified school construction bond was \$25,000,000. These bonds provide a federal subsidy to the District which significantly decreases overall interest cost. The annual requirements to amortize Measure A Series 2010 general obligation bonds payable outstanding as of June 30, 2013, are as follows:

Fiscal Year Ended June 30,	Principal	Interest	Federal Subsidy	Interest Payment	Total
2014	\$ -	\$ 1,418,755	\$ (1,332,718)	\$ 86,037	\$ 172,074
2015	-	1,418,755	(1,332,718)	86,037	172,074
2016	-	1,418,755	(1,332,718)	86,037	172,074
2017	-	1,418,755	(1,332,718)	86,037	172,074
2018	-	1,418,755	(1,332,718)	86,037	172,074
2019-2023	3,230,000	6,961,326	(6,531,141)	430,185	4,090,370
2024-2028	21,770,000	4,625,277	(4,276,510)	348,767	22,467,534
Total	\$ 25,000,000	\$ 18,680,378	\$ (17,471,241)	\$ 1,209,137	\$ 27,418,274

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements, continued
June 30, 2013**

NOTE 6 – MEASURE A – STRONG SCHOOLS BOND GENERAL OBLIGATION BONDS (continued)

Series 2013 General Obligation Bond

As of June 30, 2013, the principal balance outstanding on the Measure A Series 2013 general obligation bonds was \$70,000,000. The annual requirements to amortize Measure A Series 2013 general obligation bonds payable outstanding as of June 30, 2013, are as follows:

Fiscal Year Ended June 30,	Principal	Interest	Total
2014	\$ -	\$ 1,677,794	\$ 1,677,794
2015	15,450,000	1,994,988	17,444,988
2016	1,500,000	1,817,988	3,317,988
2017	1,810,000	1,759,288	3,569,288
2018	1,700,000	1,697,588	3,397,588
2019-2023	7,695,000	7,449,138	15,144,138
2024-2028	-	6,821,438	6,821,438
2029-2033	9,150,000	6,201,188	15,351,188
2034-2037	32,695,000	2,620,694	35,315,694
Total	\$ 70,000,000	\$ 32,040,104	\$ 102,040,104

NOTE 7 – MEASURE A – STRONG SCHOOLS BOND EXPENDITURES BY PROJECT

The following table presents the expenditure amounts by project for the fiscal year ended June 30, 2013:

Project	Amount
Duveneck Elementary School	\$ 530,388
Fairmeadow Elementary School	2,257,802
Ohlone Elementary School	405,137
Jordan Middle School	9,443,713
Terman Middle School	6,076,058
J.L.S. Middle School	9,785,661
Gunn High School	16,552,688
Palo Alto High School	16,325,077
Technology - District Wide	2,264,654
Program Administration - District Wide	1,933,068
Total	\$ 65,574,246

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Notes to Financial Statements, continued
June 30, 2013**

NOTE 8 – COMMITMENTS AND CONTINGENCIES

Litigation

On July 12, 2011, the Board of Education approved a contract with Taisei Construction Corporation in the amount of \$25,150,000 for the construction of a new classroom building and a media arts building on the Palo Alto High School campus. Completion of construction was anticipated for June 2013, but as of the date of this report the buildings have not yet been completed. The latest schedule from Taisei calls for a completion date of January 17, 2014.

On April 25, 2013, Taisei Construction Corporation filed a government code claim in the amount of \$1,653,169. The claim had previously been the subject of mediation with the District. The Board of Education rejected that claim on May 28, 2013. Taisei Construction Corporation filed a complaint in Santa Clara County Municipal Court for the claimed amount. This complaint was amended twice and was served on the District on August 30, 2013.

**OTHER INDEPENDENT
AUDITORS' REPORTS**

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

Independent Auditors' Report

Governing Board Members and
Measure A Citizens' Oversight Committee
Palo Alto Unified School District
Palo Alto, California

We have audited, in accordance with the 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, the financial statements of the Measure A - Strong Schools Bond, as of and for the year ended June 30, 2013 and the related notes to the financial statements, which collectively comprise the Measure A - Strong Schools Bond's basic financial statements, and have issued our report thereon dated September 22, 2013.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Measure A - Strong Schools Bond's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Measure A - Strong Schools Bond's internal control. Accordingly, we do not express an opinion on the effectiveness of the Measure A - Strong Schools Bond's internal control.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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Michael Ash, CPA

Heather Daud

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Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

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

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Christy White Associates

San Diego, California
September 22, 2013

INDEPENDENT AUDITORS' REPORT ON PERFORMANCE

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State Board of Accountancy*

Governing Board Members and
Measure A Citizens' Oversight Committee
Palo Alto Unified School District
Palo Alto, California

Report on the Financial Statements

We have audited the accompanying financial statements of the Measure A - Strong Schools Bond, as of and for the year ended June 30, 2013 and the related notes to the financial statements, which collectively comprise the Measure A - Strong Schools Bond's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express 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 financial statements are free from material misstatement.

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

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

In connection with our audit, we also performed an audit for compliance as required in the performance requirements for the Measure A General Obligation Bonds for the fiscal year ended June 30, 2013. The objective of the examination of compliance applicable to the District is to determine with reasonable assurance that:

- The proceeds of the sale of the Measure A Bonds were only used for the purposes set forth in the Measure A ballot language and not for any other purpose, such as teacher and administrative salaries.
- The Governing Board of the District, in establishing the approved projects set forth in the ballot measure, evaluated the remodeling, new construction and renovations of items which will improve learning and to accommodate growth in the District, with no funds expended on administrator salaries.

In performing our audit of compliance, we performed procedures including but not limited to those listed as follows:

Internal Control Evaluation

Procedures Performed:

Inquiries were made of management regarding internal controls to:

- Prevent fraud or waste regarding Measure A projects, including budgetary controls
- Ensure adequate separation of duties exists in the fiscal services department for Measure A funds
- Prevent material misstatements in the financial statements
- Ensure expenditures are allocated to the proper fund(s)
- To follow applicable regulations, including regulations related to bidding and contract management

We then performed substantive tests of financial statement balances to determine whether the controls designed by management were operating effectively, and to provide reasonable assurance that the fiscal year 2012-13 financial statement balances for the Measure A - Strong Schools Bond are not materially misstated.

Results of Procedures Performed:

The result of our audit tests show that internal control procedures appear to be working to meet the financial and compliance objectives required by generally accepted accounting standards and applicable laws and regulations. An unqualified opinion was expressed on the financial statements.

Facilities Site Walk

Procedures Performed:

We performed a site walk to verify that Measure A – Strong Schools Bond funds expended for the fiscal year ended June 30, 2013 were for valid facilities acquisition and construction purposes. We toured seven District construction sites where 2012-13 construction work occurred: Gunn High School; Palo Alto High School; Jordan Middle School; J.L.S. Middle School; Terman Middle School; Duveneck Elementary School and Fairmeadow Elementary School.

Results of Procedures Performed:

Results of the site walks indicate that the major 2012-13 Measure A – Strong Schools Bond construction projects were successfully completed and advanced into 2013-14 expenditure/construction phases where applicable.

Test of Expenditures

Procedures Performed:

The following performance tests of expenditures and transfers were performed:

1. We tested expenditures to determine whether Measure A – Strong Schools Bond funds were spent solely on voter and Board approved school facilities projects (as set forth in the District's Facilities Master Plan and the Measure A ballot measure language). The expenditure test included a sample of 84 payments, of which 74 were vendor payments and 10 were payroll payments, totaling \$23.2 million, or approximately 35% of total Measure A expenditures for 2012-13.
2. We also tested payments made to 7 professional service firms. We obtained the contracts for these firms and ensured that position rates per contract were accurately billed to the District. In addition, for program management, we analyzed the billing rates and hours charged as compared to other school districts' program management agreements.

Results of Procedures Performed:

We found all expenditures tested to be in compliance with the terms of the Measure A – Strong Schools Bond ballot measure and applicable state laws and regulations, without exception. Also, our analysis indicated that the District is receiving program management services that are reasonable as compared to other school districts, with regard to billing rates, hours charged, and the ratio of consultants to District employees. Furthermore, it appeared that the District's site projects were competitive in price with similar projects size and scope to other school construction bond programs included in our benchmarking.

Test of Contracts and Bid Procedures

Procedures Performed:

For the fiscal year ended June 30, 2013, we performed testing of eight contracts to determine compliance with District policy and Public Contract Code provisions related to contracting and bidding:

Formal Bids

- Project: Duveneck Elementary School Modernization and New Construction
Original Contract Award Amount: \$6,626,874 (base bid)
- Project: JLS Landscape and Site Improvement
Original Contract Award Amount: \$776,000
- Project: Palo Alto High School Synthetic Track
Original Contract Award Amount: \$162,990
- Project: Gunn High School Gym Modernization
Original Contract Award Amount: \$795,000 (base bid)

Informal Bids

- Project: Palo Alto High School Portables (BP#1 Cabinets)
Original Contract Award Amount: \$84,000
- Project: Palo Alto High School Portables (BP#2 Site and Indoor Plumbing)
Original Contract Award Amount: \$42,500
- Project: Palo Alto High School Portables (BP#3 General)
Original Contract Award Amount: \$39,995
- Project: Palo Alto High School Portables (BP#4 Electrical & Data)
Original Contract Award Amount: \$24,553

Results of Procedures Performed:

We found that the contracts tested above for bidding procedures followed proper bidding procedures and were awarded in all cases to the lowest responsible bidder, except as noted in the accompanying schedule of findings and responses as finding #2013-1.

In addition, we tested nine change orders and determined the change orders were executed in accordance with District internal controls and were in compliance with applicable provisions of the Public Contract Code. Contracts tested with change orders included the following projects: Jane Lanthrop Stanford Middle School Modernization and New Construction, David Starr Jordan Middle School Modernization and New Construction, Terman Middle School Modernization and New Construction, Gunn High School New Gymnasium, Gunn High School New Classroom Buildings A & B, Oholone Elementary School Modernization and New Construction, Air Conditioning of Existing Classrooms. Moreover, we noted that the District has been providing the Governing Board with a listing of change orders to contracts that relate to Measure A – Strong Schools Bond projects in fiscal year 2012-13 and that no Measure A projects have a cumulative change order rate in excess of 10% of contract value.

Citizens' Oversight Committee

Procedures Performed:

In accordance with AB 1908 (Assembly Bill) and Ed Code Section 15278, the District is required to establish a bond oversight committee for Prop 39 bonds including one active member from each of the following sectors: a business organization, senior citizens organization, bona fide taxpayers association, and one parent/guardian of a child enrolled in the District and one parent/guardian of a child enrolled in the District who is also a member of a parent teacher association. The COC is to meet pursuant to Education Code Section 15280.

Results of Procedures Performed:

In our review of the minutes of the Citizens' Oversight Committee for Measure A, we found that there was adequate documentation of meetings held during fiscal year 2012-13. In addition, the District has submitted annual audit reports during the life of the Measure A – Strong Schools Bond.

In our review of the composition of the committee, we noted that the District has the proper members in the COC that come from each of the sectors noted above.

Our audit of compliance was made for the purposes set forth in the second and third paragraphs of this report and would not necessarily disclose all instances of noncompliance.

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

Opinion

In our opinion, based on the fieldwork described above as well as the other tests that we conducted, the District complied with the compliance requirements for the Measure A – Strong Schools Bond as listed and tested above, except as noted in the accompanying schedule of findings and responses as finding #2013-1.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on accountability requirements pursuant to the passage of Proposition 39 and the enactment of AB 1908 (Chapter 44, Statutes of 2000). Accordingly, this report is not suitable for any other purpose.

Christy White Associates

San Diego, California
September 22, 2013

FINDINGS AND RESPONSES SECTION

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Schedule of Findings and Responses
For the Fiscal Year Ended June 30, 2013**

This section identifies the deficiencies, significant deficiencies, material weaknesses, and instances of noncompliance related to the financial statements that are required to be reported in accordance with *Government Auditing Standards*.

FINDING #2013-1: INFORMAL BIDDING PROCEDURES

Criteria: The California Uniform Public Cost Accounting Act (Public Contract Code Section 2200) requires that the District submit one trade journal advertisement to all four of the required trade journals on an annual basis related to the informal bidding process.

Condition: During our testing of awards of contracts subject to the informal bid procedures in 2012-13, we noted that the District could not provide verification that they submitted the trade journal advertisement to all four required trade journals as required by California Uniform Public Cost Accounting Act (CUPCAA). The finding affected 4 (100%) of informal bid contracts tested in 2012-13.

Cause: The District did not maintain supporting documents to provide proof that the advertisement was submitted to the required trade journals.

Effect: Noncompliance with CUPCAA.

Questioned Costs: None.

Recommendation: The District should ensure that all informal bid advertisements are properly submitted to the required trade journals in accordance with CUPCAA. In addition, the District should maintain support such as fax confirmations or email confirmations that the advertisements were submitted.

District Response: The District will ensure proper documentation of the required trade journal advertisements going forward. This exception is partially compensated for, as the District advertises in the required trade journals each time that a project is put out to formal bid, in addition to the annual notice. The advertisements for these projects have been tested and confirmed by our auditors in the Test of Contract and Bid Procedures section of this report.

**MEASURE A – STRONG SCHOOLS BOND
PALO ALTO UNIFIED SCHOOL DISTRICT
Summary Schedule of Prior Audit Findings
For the Fiscal Year Ended June 30, 2013**

Our tests resulted in no findings and recommendations related to the financial and performance audit of the Measure A – Strong Schools Bond for the fiscal year ended June 30, 2012