To the Audit Committee
Kirtland Community College

Dear Audit Committee Members:

We have audited the financial statements of Kirtland Community College (the “College), including its component unit, The Foundation, as of and for the year ended June 30, 2013 and have issued our report thereon dated October 11, 2013. Professional standards require that we provide you with the following information related to our audit which is divided into the following sections:

Section I - Communications Required Under AU 260

Section II - Other Recommendations and Related Information

Section I includes information that current auditing standards require independent auditors to communicate to those individuals charged with governance. We will report this information annually to the audit committee of the College.

Section II includes information offered in the interest of helping the College in its efforts toward continuous improvement, not just in the areas of internal control and accounting procedures, but also in operational or administrative efficiency and effectiveness.

We would like to take this opportunity to thank Jason Broge, Ilene Scherer, and all the College’s staff for the cooperation and courtesy extended to us during our audit. Their assistance and professionalism are invaluable.

This report is intended solely for the use of the audit committee and management of the College and is not intended to be and should not be used by anyone other than these specified parties.
To the Audit Committee
Kirtland Community College

October 11, 2013

We welcome any questions you may have regarding the following communications and we would be willing to discuss any of these or other questions that you might have at your convenience.

Very truly yours,

Plante & Moran, PLLC

Michael Schrage, CPA
Partner

Katie A. Thornton, CPA
Associate
Section I - Communications Required Under AU 260

Our Responsibility Under U.S. Generally Accepted Auditing Standards

As stated in our engagement letter dated August 27, 2013, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities. Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

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

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

Our audit of Kirtland Community College’s financial statements has also been conducted in accordance with Government Auditing Standards, issued by the Comptroller General of the United States. Under Government Auditing Standards, we are obligated to communicate certain matters that come to our attention related to our audit to those responsible for the governance of Kirtland Community College, including compliance with certain provisions of laws, regulations, contracts, grant agreements, certain instances of error or fraud, illegal acts applicable to government agencies, and significant deficiencies in internal control that we identify during our audit. Toward this end, we issued a separate letter dated October 11, 2013 regarding our consideration of Kirtland Community College’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our meeting about planning matters on June 6, 2013.

We recognize the relationship between the Director of Accounting and Director of Institutional Services. We have tailored our audit procedures to address this risk.
Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the College are described in Note 1 to the financial statements. As described in Note 1, the College adopted new accounting policies related to the financial reporting presentation of certain items described as deferred inflows, deferred outflows, and net position. These changes are the result of GASB 63 and GASB 65. Accordingly, the new accounting policies adopted have been retrospectively applied to prior periods presented as if the policy had always been used. We noted no transactions entered into by the College during the year for which there is a lack of authoritative guidance or consensus.

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

Accounting estimates are an integral part of the financial statements prepared by management and are based on management’s knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements are summarized below:

- Management’s estimate of the fair value of the College’s investments. We tested the fair values for a sample of investments by comparing recorded prices to quoted market prices and concur with management’s valuation.

- Management estimates fair value of tuition accounts receivable by establishing an allowance for estimated uncollectible amounts. We evaluated the allowance for uncollectible accounts to determine the amounts recorded are reasonable.

- Management estimates the scholarship allowances for tuition revenue using a historical relationship between financial aid awarded for books in excess of the associated tuition revenue. We evaluated this estimate and agree with management that it was reasonable in relation to the overall financial statements.

The disclosures in the financial statements are neutral, consistent, and clear. Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosure affecting the financial statements was in Note 3, which summarizes cash and investments by risk.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing and completing our audit.
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**Disagreements with Management**

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

**Corrected and Uncorrected Misstatements**

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

Management has corrected all such misstatements to implement a full accrual basis of accounting for Kirtland Community College Foundation (a discretely presented component unit). Management has determined the effects of the FASB prescribed endowment footnote disclosure related to Foundation activity are immaterial to the financial statements taken as a whole.

**Significant Findings or Issues**

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

**Management Representations**

We have requested certain representations from management that are included in the management representation letter dated October 11, 2013.

**Management Consultations with Other Independent Accountants**

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

Our responsibility for other information in documents containing the entity’s financial statements and report does not extend beyond the financial statements. We do not have an obligation to determine whether or not such other information is properly stated. However, we read the management’s discussion and analysis and nothing came to our attention that caused us to believe that such information, or its manner of presentation, is materially inconsistent with the information or manner of its presentation appearing in the financial statements.
Section II - Other Recommendations and Related Information

IRS Issues Tax Identification Number Notifications

Recently the Internal Revenue Service (IRS) started issuing notices to many higher education colleges regarding various information returns, including Forms 1099 and 1098T. The notice is a result of a matching program instituted by the IRS that identifies when the taxpayer identification number is missing or incorrect based on the IRS database. It is important to respond to the notice timely. Penalties can be significant. Penalties can be removed if the failure to file a complete document was due to reasonable cause and not willful neglect.

Recommended steps to gather information necessary to establish reasonable cause:

- Review the information included with the notice that provides the details of each error identified and compare the information to the records maintained by the organization. Break the forms down by type of return and then by type of error.

- Forms with identification numbers that do not agree to the IRS database need to be further broken down into two sub groups. The first group should be the returns where the number was entered into the system incorrectly due to an administrative oversight. The second group would be those forms where an incorrect identification number was provided by the recipient. Documentation should be gathered to support the findings.

- Forms with missing identification numbers will require additional documentation. Ideally the organization has maintained the documentation to support the efforts made in each instance to obtain the necessary information. Any subsequent follow up documentation may further support the efforts made by the College.

- The College should consider prior year filings and look to see if in the past amended forms were filed with the correct information obtained subsequent to filing. This information can support that the College continues to seek the necessary information and, when obtained, amends the returns accordingly.

- If the College has procedures in place to identify errors and to prevent filing returns with missing tax identification numbers, it may be advisable to attach a copy of the procedures or make reference to them in your response.

We recognize that each college is different and each error identified may have a unique set of facts and circumstances. For additional information, a full article is available at www.plantemoran.com/perspectives.
Affordable Care Act - In 2010, the Patient Protection and Affordable Care Act (PPACA) was passed in an effort to reduce the cost of health care, extend care to virtually all Americans, and improve the delivery and quality of health care. Since becoming effective, many parts of the law have been enacted. On or around July 2, 2013, the Administration announced that it would provide an additional year before the Affordable Care Act (ACA) mandatory employer and insurer reporting requirements begin, which effectively delayed the employer shared responsibility payments (play or pay mandate) until 2015. Employers should take care and consider an advance strategy to ensure compliance with PPACA so that application of any penalties due to noncompliance with the play or pay/shared responsibility mandates is avoided.

The Patient Protection and Affordable Care Act (PPACA) sets forth a number of requirements that large employers need to consider in order to avoid the potential assessment of penalties due to noncompliance. Here are a few questions the College should consider:

- Are you certain that your organization’s eligibility rules meet the requirements of PPACA (staff working 30 or more hours/week)?
- Have you evaluated the plans that are available to ensure they satisfy the minimum essential coverage requirements (are all the required coverage elements included at or above the minimum values)?
- Are your plans affordable, as defined by the law?

NACUBO’s Blank Slate Project - The Blank Slate Project is an effort of NACUBO’s Accounting Principles Council (APC), inspired by the FASB’s Not-for-Profit Advisory Committee to produce a single reporting model for higher education that is not FASB or GASB specific. The project’s objective is to focus on what users really want to know about higher education colleges. Following is a summary of their plans to date:

Net Assets to be reclassified as resources that can be further divided into five sub-categories:

- Undesignated resources: resources to fulfill the mission of the College in future periods
- Net investment in plant: net book value of all capital assets offset by outstanding liabilities associated with those capital assets.
- Board-designated resources: for long-term purposes such as additions to capital, repayment of debt, etc.
- Third-party designated resources: external party has restricted the use
- Endowment resources: true and quasi-endowments; annuity and life income funds subject to donor-imposed restrictions.

Promises to give (pledges) by external parties that do not carry designations are currently recorded as pledges pending cash receipt until the donor honors their promise. The proposed change by NACUBO is to recognize revenue when the gift is received. This has not been approved by the GASB, and the FASB stands by recognizing pledges when promised.
A proposed change for current statements to look more like those of a ‘for profit’; using the terms “balance sheet” and “income statement” for uniformity. Revenue to be broken into two categories: current support revenue and fee for service and expenses classified more naturally, thinking about trustees as business members.

Introducing a new financial statement, “Changes in Resources,” that will rollforward each component of net assets year to year, categorized like a cash flow statement.

Expanding disclosures to provide functional expense definitions with a table crosswalk of natural to functional classification; additional details on discounting separate from student tuition revenue, and maturity of investments.

The proposed next steps by the Accounting Principles Council will include a test run of the changes along with a focus group discussion with other colleges.

(Michigan) MPSERS Reforms - On September 5, 2012, Public Act #300 (or Senate Bill 1040) was signed into law by the governor. The law outlines significant reforms to the MPSERS retirement system that will dramatically affect the expected retirement rates paid by the College as well as the benefits provided to MPSERS participants.

One of the reforms was to cap the employer’s share of the unfunded actuarial accrued liability (UAAL) on reported payroll at 20.96 percent. As a result, the balance of retirement costs will be funded with state appropriations, referred to as the MPSERS UAAL Rate Stabilization payments. For the years ended June 30, 2013 and 2014, the College will receive approximately $158,000 and $396,000, respectively.

Accounting for Pension and Other Postemployment Benefits (OPEB) - In June 2012, the Governmental Accounting Standards Board (GASB) issued GASB Statement No. 68, Accounting and Financial Reporting for Pensions. Under GASB No. 68, the College, as a cost-sharing employer, will be required to recognize its proportionate share of the collective unfunded net pension liability, pension expense, and deferred pension outflows (inflows) of the Michigan Public School Employees’ Retirement System (MPSERS) plan within its financial statements. This will be a significant change for every community college and K-12 school district in the State of Michigan. Michigan community colleges will see a significant liability reflected on their balance sheets along with significant increases to pension expenses and a corresponding reduction to unrestricted net assets. The College has estimated its proportionate share of the unfunded net pension liability to be approximately $19.6 million. The provisions of this statement are effective for financial statements for the year ending June 30, 2015. Please see Appendix A for additional details regarding these changes.
It is important to note that GASB No. 68 does not change the accounting and reporting for the retiree health care component of the MPSERS plan (OPEB). However, the GASB does have a separate project to address OPEB which we anticipate will result in similar accounting and reporting. The GASB’s current OPEB project work plan calls for a public comment period on the exposure draft from September to November 2013 with a planned final issuance of the standard in June 2014.

Appendix A:

(Michigan) Accounting for Michigan Public Schools Employees’ Retirement System (MPSERS) - In June 2012, the GASB issued a standard addressing accounting for pension plans that will impact the College. The new standards will result in significant changes to how the College accounts for its participation in the Michigan Public Schools Employees’ Retirement System (MPSERS).

Key points are as follows:

- Under existing GASB rules, colleges participating in the MPSERS, described as cost-sharing employers, currently report no liability for the unfunded pension obligations of that plan. Employer contributions are expensed when the corresponding wages used to determine the contribution are earned by the employee (essentially “pay and expense as you go”).

- Under GASB No. 68, the College, as a cost-sharing employer, will recognize its proportionate share of the collective unfunded net pension liability, pension expense, and deferred pension outflows (inflows) of the MPSERS plan. These amounts will be reported in the College’s financial statements.

- The method of allocating this liability to each participating employer has not yet been determined, so the precise impact is not known. However, a high level approach to estimating the liability is based on the unfunded actuarial accrued liability reported in the MPSERS’ September 30, 2012 financial statement and allocated based on the College’s covered payroll as a percentage of the total MPSERS plan covered payroll.

- The footnote disclosure requirements will be more extensive, including 10-year schedules that will be required to be presented as required supplemental information. As a result, it likely will be time-intensive to compile.

- The provisions of this statement are effective for financial statements for the year ending June 30, 2015 and will require the liability for the College’s proportionate share to be recorded at that time. For the 2012-2014 financial statements, the College has the option to designate unrestricted, undesignated net assets in anticipation of recording the liability in 2015.

- In August 2012, the GASB announced a project work plan to issue an implementation guide focused on issues related to employer-specific requirements of the standard. The guide is scheduled for issuance in January 2014.
GASB Fair Value Measurement - On June 20, the Governmental Accounting Standards Board (GASB) issued a “Preliminary Views” (PV) document entitled “Fair Value Measurement and Application,” that focuses on fair value measurement and note disclosures. A PV is a board document used to solicit feedback on complex matters in the early stages of a technical project; a PV is an important step toward an exposure draft of a statement.

The objectives of the GASB’s project on fair value measurement and application are to study attributes of fair value, establish a measurement framework for fair value, define fair value, provide guidance for applying fair value measurements to assets and liabilities, and recommend appropriate disclosures.

Other Opportunities for Change

Fraud Prevention and Detection - Over the last decade, issues related to fraud have received increased attention and colleges are no exception. As each college visits the issues related to fraud, two key questions are often repeated. They are:

• Could this have happened here?
• How can we prevent it?

These questions are essential in any evaluation of a college’s internal control system. In fact, they are the cornerstone for developing or redesigning any internal control process, including controls over the safeguarding of college assets and the capturing and reporting of college information. In short, to design effective controls, both the Board of Trustees and administration must consider where the potential for fraud might exist and what practical/reasonable means should be put in place to deter it from occurring and detect it if it does occur.

Three foundational elements exist in most instances of fraud. They are:

• Incentive (the reason to commit a fraud)
• Opportunity (the ability to commit the fraud)
• Rationalization/Attitude (the view of the world that makes the fraud acceptable)

Generally, it is necessary for all three to be present to experience a fraud. In any case, the College can significantly impact one of the three elements - “opportunity”. This area is where the College can thwart fraudulent schemes by implementing strong internal controls.

To the degree that the College effectively identifies where “opportunity” may exist for fraud and implements controls to prevent and/or detect it, the likelihood of fraud occurring is greatly reduced.
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The public accounting profession also has increased its focus in the fraud area. Auditors apply the auditing standard, Statement on Auditing Standard #99 (SAS #99), Consideration of Fraud, in a financial statement audit. The focus of this audit standard is on detection of fraud that is material (significant) to the College’s financial statements. In completing this audit requirement, we will be evaluating the College’s process for identifying areas for potential significant fraud (both in the area of misappropriation of College assets as well as financial statement misstatement) and the related controls put in place to prevent and/or detect it.

While colleges have often evaluated and revised internal controls within the college, the expectations related to fraud might pose unique challenges for the Board of Trustees and administration. We have continued to maintain a Top 10 listing of items for colleges to consider, as well as specific items related to certain transaction cycles (cash receipts, disbursements, and payroll). We would be happy to discuss these items with you at your convenience.

Fraud prevention and detection is clearly a joint effort and it is our hope these items will aid the College in responding to the fraud concerns that seem to surround us all.

**CRESA Project Management (Owner’s Representative)** - Designing and constructing a new facility or renovating an existing facility is an exciting yet difficult time for a college. The benefits of engaging a project manager (owner’s representative) to assist the college in the management of the project should be considered. Questions could include:

- Should the project be delivered through a general contractor for a fix fee or a construction manager for a cost plus fee?
- Who in the college is qualified to approve change orders?
- Is an interior design firm necessary or will that be provided by the architect and at what cost?
- Who will be handling furniture procurement?
- What are the pros and cons of a wood truss shingle roof versus a flat rubber roof?
- Who in the college is qualified and has the time to write all the RFPs and provide the bid analysis on a comparable basis?

These and more difficult questions will arise and the decisions made will have a long-lasting effect on the College, both structurally and financially.

Plante & Moran CRESA, LLC (P&M’s “Corporate Real Estate Service Advisors”) provides project management services with its sole fiduciary to its clients (zero conflicts of interest) and implements a multi-step process in which the services are delivered from project conception to completion. Key processes are managed with a multi-disciplined team of architects, engineers, strategic consultants, financial advisors, and real estate professionals in order to maximize the client’s facilities by keeping a project on schedule, on budget and constructed with the highest level of quality. The key processes that are managed (either in totality or allocated) are as follows:

- Building needs assessment (programming, construction cost estimates, etc.)
- Procure land and manage due diligence (i.e., soil borings, surveys, etc.)
- Assemble design team (i.e., pre-qualify, write RFP, etc.)
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- Manage design process (i.e., critique documents, value engineering, etc.)
- Assemble construction team (i.e., bid analysis, negotiate contract, etc.)
- Manage construction process (i.e., contractor oversight, change order management, etc.)
- Closeout project (i.e., furniture procurement, move management, etc.)

If you are contemplating construction or renovation projects, we would be happy to discuss our capabilities in this area and the value we can bring to the process.

**Network Security Assessment** - Security breaches at schools have made headlines recently, with students obtaining access to grade books and future tests among other items. Hacking tools have become more prevalent and easier to obtain. Given the increased sensitivity to privacy and increased reliance on networks, the College should consider an independent network security assessment to evaluate potential risks and obtain recommendations for increasing security. A thorough review of the College’s access points, risk, and exposure should be conducted to ensure the continued secured operation of the College’s network and systems.

**Technology Support Assessment** - Your College has recently implemented a significant amount of technology or has changed the way technology is used to support instruction and administrative systems. A technology support assessment may be appropriate at this point to ensure that the College has the appropriate support mechanisms in place. A Technology Support Assessment addresses technology policies and procedures, IT department organization, staffing requirements, job descriptions and associated salaries, training requirements, and appropriate level of contracted services.