

**PROPOSITION K BOND BUILDING FUND OF  
SAN MARCOS UNIFIED SCHOOL DISTRICT**

**AUDIT REPORT**

**For the Fiscal Year Ended  
June 30, 2012**



**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
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June 30, 2012**

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**PROPOSITION K BOND BUILDING FUND  
 SAN MARCOS UNIFIED SCHOOL DISTRICT  
 Introduction and Citizens' Bond Oversight Committee Member Listing  
 June 30, 2012**

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San Marcos Unified School District (the "District") operates eleven elementary schools, three middle schools, two comprehensive high schools, a continuation high school, an independent study high school, and an adult school. The District serves approximately 18,250 students.

In November 2010, the voters of the District approved, by more than the required 55% favorable vote, Proposition K, authorizing the issuance and sale of general obligation bonds, not to exceed \$287,000,000. Proposition K 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 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 facilities projects.

Proposition K bonds were issued by the District, through the County of San Diego. On June 22, 2011, the District issued Series A of the Election of 2010 General Obligation Bonds in the amount of \$142,046,476. On April 25, 2012, the District issued Series B of the Election of 2010 General Obligation Bonds in the amount of \$64,995,522.

The accompanying Proposition K Audit Report, for the fiscal year ended June 30, 2012, reflects the issuance of Series A and B of the Proposition K general obligation bonds and compliance with the applicable requirements of Proposition 39 for such period.

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 Proposition K including formation, composition and purpose of the Citizens' Oversight Committee. In compliance with Education Code Section 15278(a), the Proposition K Citizens' Oversight Committee was formed within 60 days of January 10, 2011, the date that the governing board entered the Proposition K election results on its minutes pursuant to Section 15274.

The Proposition K Citizens' Oversight Committee was comprised of the following members as of June 30, 2012:

<b>Name</b>	<b>Title</b>	<b>Representation</b>
William Effinger	Chair	Senior Citizens' Organization
Michael Brock	Vice Chair	Parent
Darius Khayat	Clerk	At-Large Member
Mike McDowell	Member	Taxpayer's Organization
Stephanie Nunez	Member	Parent & PTA Organization
Anthony Martindale	Member	Business Organization
David Barnum	Member	At-Large Member
Tom Kumura	Alternate	At-Large Member
Joseph Potts	Alternate	At-Large Member

INDEPENDENT AUDITORS' REPORT

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Governing Board Members and  
Proposition K Citizens' Bond Oversight Committee  
San Marcos Unified School District  
San Marcos, California

We have audited the accompanying balance sheet of the Proposition K Bond Building Fund of San Marcos Unified School District (the "District") as of June 30, 2012, and the related statement of revenues, expenditures and changes in fund balance for the fiscal year ended June 30, 2012. 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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.

As discussed in Note 1A, the financial statements present only the individual Proposition K Bond Building Fund, consisting of the net construction proceeds of Proposition K Series A and B general obligation bonds as issued by the District, through the County of San Diego, and are not intended to present fairly the financial position of the District in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Proposition K Bond Building Fund of San Marcos Unified School District as of June 30, 2012, and the results of its operations for the fiscal year ended June 30, 2012, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated January 10, 2013, on our consideration of San Marcos Unified School 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. The purpose of that report is to describe the scope of our testing of internal controls over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

*Christy White Associates*

San Diego, California  
January 10, 2013

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# FINANCIAL SECTION

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**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Balance Sheet  
June 30, 2012**

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<b>ASSETS</b>	
Cash	\$ 174,117,243
Accounts receivable	139,928
Due from other funds	<u>97,104</u>
<b>Total Assets</b>	<b>\$ <u>174,354,275</u></b>
<b>LIABILITIES AND FUND BALANCE</b>	
<b>Liabilities</b>	
Accounts payable	3,353,362
Due to other funds	<u>7</u>
<b>Total Liabilities</b>	<b><u>3,353,369</u></b>
<b>Fund Balance</b>	
Restricted for capital projects	<u>171,000,906</u>
<b>Total Liabilities and Fund Balance</b>	<b>\$ <u>174,354,275</u></b>

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

**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Statement of Revenues, Expenditures and Changes in Fund Balance  
For the Fiscal Year Ended June 30, 2012**

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<b>REVENUES</b>	
Interest income	\$ 617,075
Other local revenue	17,668
<b>Total Revenues</b>	<u>634,743</u>
<b>EXPENDITURES</b>	
Plant services	89,307
Facilities acquisition and construction	33,807,652
Transfers to other agencies	46,700
Debt service - interest and other	2,478,782
<b>Total Expenditures</b>	<u>36,422,441</u>
<b>Excess (Deficiency) of Revenues Over (Under) Expenditures</b>	<u>(35,787,698)</u>
<b>OTHER FINANCING SOURCES (USES)</b>	
Proceeds from long-term debt	209,748,100
Transfers out	(6,146,801)
<b>Total Other Financing Sources</b>	<u>203,601,299</u>
<b>Net Change in Fund Balance</b>	167,813,601
<b>Fund Balance, July 1, 2011</b>	<u>3,187,305</u>
<b>Fund Balance, June 30, 2012</b>	<u>\$ 171,000,906</u>

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



**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Notes to Financial Statements  
June 30, 2012**

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**NOTE 1 – SIGNIFICANT ACCOUNTING POLICIES**

**A. Reporting Entity**

The Board of Supervisors of San Diego County adopted a resolution on May 27, 1975, creating a new unified school district comprising the area of Rich-Mar Union School District named “San Marcos Unified School District.” The District operates eleven elementary schools, three middle schools, two comprehensive high schools, a continuation high school, an independent study high school, and an adult school. The District serves approximately 18,250 students.

In November 2010, the voters of the District approved by more than 55% Proposition K, authorizing the issuance and sale of general obligation bonds, not to exceed \$287,000,000, for the construction, reconstruction, rehabilitation or replacement of school facilities, including the furnishing and equipping of school facilities, or the acquisition or lease of real property for school facilities.

An advisory committee to the District’s Governing Board and Superintendent, called the Proposition K Citizens’ Oversight Committee, was established pursuant to the requirements of state law and the provisions of Proposition K. According to its mission statement, the Committee’s oversight goals include: providing independent monitoring and review of all Proposition K fund expenditures in accordance with contracts executed by and between the District, its Contractors and Sub-contractors and all Bond Agency requirements and to keep the public informed through normal public information channels.

The statements presented are for the individual Proposition K Bond Building Fund of the District, consisting of the net construction proceeds of Proposition K Series A and B general obligation bonds as issued by the District, through the County of San Diego, 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).

**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Notes to Financial Statements, continued  
June 30, 2012**

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**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. On a 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.

**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 San Diego 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.

**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Notes to Financial Statements, continued  
June 30, 2012**

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**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 the Proposition K 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.

**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Notes to Financial Statements, continued  
June 30, 2012**

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**NOTE 2 – CASH AND INVESTMENTS**

**Summary of Cash and Investments**

Cash and investments as of June 30, 2012 are classified in the accompanying financial statements as cash in county treasury of \$174,077,336 and cash with fiscal agent of \$39,907.

**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.

*Cash with Fiscal Agent* - Cash with Fiscal Agent represents \$39,907 held by US Bank and restricted for construction costs relating to the Proposition K bond.

**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Notes to Financial Statements, continued  
June 30, 2012**

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**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

**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Notes to Financial Statements, continued  
June 30, 2012**

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**NOTE 2 – CASH AND INVESTMENTS (continued)**

Limitations as they relate to interest rate risk, credit risk, custodial 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.

<b>Investment Type</b>	<b>Fair Value</b>	<b>Maturity</b>
County Treasury	\$ 174,582,160	370 days

**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. The investment in the San Diego County Investment Pool is rated AAAsf/S1 by Standard & Poor's.

**Custodial Credit Risk**

Custodial credit risk is the risk that, in the event of a failure of a counterparty to an investment, some or all of the investment amount may not be recovered by the holder of the investment. The District's investments as of June 30, 2012 were not subject to custodial credit risk because the investments were in the county investment pool.

**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.

**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Notes to Financial Statements, continued  
June 30, 2012**

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**NOTE 3 – PROPOSITION K GENERAL OBLIGATION BONDS**

On March 5, 2002, the voters of the San Marcos Unified School District approved by more than 55% Proposition K, authorizing the issuance and sale of \$287,000,000 of general obligation bonds. Proposition K bonds were issued by the District, through the County of San Diego. On June 22, 2011, the District issued Series A of the Election of 2010 General Obligation Bonds in the amount of \$142,046,476. On April 25, 2012, the District issued Series B of the Election of 2010 General Obligation Bonds in the amount of \$64,995,522, resulting in total bond indebtedness of \$207,041,998, as described below:

- The 2010 Series A General Obligation Bonds consist of current interest bonds of \$116,700,000 with interest yields ranging from 2.56% to 5.10% and fully maturing on August 1, 2038 and capital appreciation bonds of \$25,346,476 with interest yields of 1.38% to 6.65%. The principal balance outstanding as of June 30, 2012 is \$142,819,864, which includes accreted interest on the capital appreciation bonds.
- The 2010 Series B General Obligation Bonds consist of capital appreciation bonds of \$64,995,522 with interest yields of 0.75% to 5.80% and fully maturing on August 1, 2051. The balance outstanding as of June 30, 2012 is \$64,995,522.

The annual requirements to amortize all Proposition K outstanding general obligation bonds payable as of June 30, 2012, presented in a consolidated format, are as follows:

<b>Fiscal Year</b>	<b>Principal*</b>	<b>Interest</b>	<b>Total</b>
2013	\$ -	\$ 6,260,200	\$ 6,260,200
2014	648,053	5,890,885	6,538,938
2015	748,008	5,920,930	6,668,938
2016	897,633	5,971,305	6,868,938
2017	1,094,562	6,049,376	7,143,938
2018-2022	10,352,982	31,924,308	42,277,290
2023-2027	14,092,908	42,495,782	56,588,690
2028-2032	30,884,699	44,851,052	75,735,751
2033-2037	61,565,491	39,783,509	101,349,000
2038-2042	41,899,999	22,665,001	64,565,000
2043-2047	17,669,111	94,900,410	112,569,521
2048-2052	27,188,552	199,897,561	227,086,113
	<b>\$ 207,041,998</b>	<b>\$ 506,610,319</b>	<b>\$ 713,652,317</b>

\*Principal does not include accreted interest of \$773,388 as of June 30, 2012.

**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Notes to Financial Statements, continued  
June 30, 2012**

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**NOTE 3 – PROPOSITION K GENERAL OBLIGATION BONDS (continued)**

The annual requirements to amortize all Proposition K outstanding general obligation bonds payable as of June 30, 2012, presented in a non-consolidated format, are as follows:

<b>Fiscal Year</b>	<b>Principal*</b>	<b>Interest</b>	<b>Total</b>
2013	\$ -	\$ 6,260,200	\$ 6,260,200
2014	648,053	5,890,885	6,538,938
2015	748,008	5,920,930	6,668,938
2016	897,633	5,971,305	6,868,938
2017	1,094,562	6,049,376	7,143,938
2018	1,299,782	6,199,156	7,498,938
2019	1,515,544	6,433,394	7,948,938
2020	2,329,381	6,099,557	8,428,938
2021	1,948,298	6,984,440	8,932,738
2022	3,259,977	6,207,761	9,467,738
2023	2,479,332	7,556,406	10,035,738
2024	2,760,909	7,879,829	10,640,738
2025	2,877,972	8,402,766	11,280,738
2026	2,947,935	9,007,803	11,955,738
2027	3,026,760	9,648,978	12,675,738
2028	2,464,010	10,971,728	13,435,738
2029	2,525,693	11,715,045	14,240,738
2030	6,477,842	8,617,896	15,095,738
2031	9,135,738	6,865,624	16,001,362
2032	10,281,416	6,680,759	16,962,175
2033	3,696,576	14,283,924	17,980,500
2034	12,296,054	6,759,446	19,055,500
2035	13,669,714	6,531,286	20,201,000
2036	15,157,181	6,257,819	21,415,000
2037	16,745,966	5,951,034	22,697,000
2038	18,450,810	5,610,940	24,061,750
2039	20,291,339	5,211,911	25,503,250
2040	1,114,150	3,885,850	5,000,000
2041	1,051,500	3,948,500	5,000,000
2042	992,200	4,007,800	5,000,000
2043	936,000	4,064,000	5,000,000
2044	874,850	4,125,150	5,000,000
2045	4,429,554	22,506,887	26,936,441
2046	5,677,168	30,834,608	36,511,776
2047	5,751,539	33,369,765	39,121,304
2048	5,712,616	35,382,384	41,095,000
2049	5,436,509	37,713,894	43,150,403
2050	5,391,404	39,919,148	45,310,552
2051	5,346,299	42,228,859	47,575,158
2052	5,301,724	44,653,276	49,955,000
	<b>\$ 207,041,998</b>	<b>\$ 506,610,319</b>	<b>\$ 713,652,317</b>

\*Principal does not include accreted interest of \$773,388 as of June 30, 2012.



**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Notes to Financial Statements, continued  
June 30, 2012**

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**NOTE 4 – ACCOUNTS RECEIVABLE**

Accounts receivable of the Proposition K Bond Building Fund consisted of \$139,928 in accrued interest as of June 30, 2012.

**NOTE 5 – INTERFUND TRANSACTIONS**

**A. Interfund Receivables/Payables (Due From/Due to)**

Interfund receivable and payable balances at June 30, 2012 consisted of \$7 due to the General Fund from the Proposition K Building Fund for PERS transfers and \$97,104 due to the Proposition K Building Fund from the General Fund for campus supervisor costs related to the construction of San Marcos High School.

**B. Operating Transfers**

Interfund transfers for the year ended June 30, 2012 consisted of a transfer from the Proposition K Building Fund to the General Fund of \$146,801 and a transfer from the Proposition K Building Fund to the Capital Facilities Fund of \$6,000,000 to reimburse for advances of capital pending funding from the initial GO Bond issuance.

**NOTE 6 – CONSTRUCTION COMMITMENTS**

As of June 30, 2012, the Proposition K Bond Building Fund had commitments with respect to unfinished capital projects of \$119,721,745.

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## **OTHER INDEPENDENT AUDITORS' REPORTS**

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**INDEPENDENT AUDITORS' 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**

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*Licensed by the California  
State Board of Accountancy*

Governing Board Members and  
Proposition K Citizens' Bond Oversight Committee  
San Marcos Unified School District  
San Marcos, California

We have audited the financial statements of the Proposition K Bond Building Fund of the San Marcos Unified School District as of and for the fiscal year ended June 30, 2012 and have issued our report thereon dated January 10, 2013. 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 Control Over Financial Reporting**

Management of San Marcos Unified School District is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered San Marcos Unified School District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the San Marcos Unified School District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the San Marcos Unified School District's internal control over financial reporting.

*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 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.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Proposition K Bond Building Fund of San Marcos Unified School District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, 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*.

This report is intended solely for the information and use of the District's Governing Board, the Proposition K Citizens' Oversight Committee, management, others within the entity, and the taxpayers of San Marcos Unified School District and is not intended to be and should not be used by anyone other than these specified parties.

*Christy White Associates*

San Diego, California  
January 10, 2013

INDEPENDENT AUDITORS' REPORT ON PERFORMANCE

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State Board of Accountancy*

Governing Board Members and  
Proposition K Citizens' Bond Oversight Committee  
San Marcos Unified School District  
San Marcos, California

We have audited the financial statements of the Proposition K Bond Building Fund of the San Marcos Unified School District (the "District") as of and for the fiscal year ended June 30, 2012 and have issued our report thereon dated January 10, 2013. Our audit was made in accordance with generally accepted auditing standards in the United States of America and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In connection with our performance audit, we performed an audit for compliance as required in the performance requirements for the Proposition K Bond Building Fund ("Proposition K") for the fiscal year ended June 30, 2012. The objective of the audit of compliance applicable to the District is to determine with reasonable assurance that:

- The proceeds from the sale of the Proposition K Bond Building Funds were only used for the purposes set forth in the ballot Proposition and not for any other purpose, such as teacher and administrative salaries.

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

<b>Internal Control Evaluation</b>
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**Procedures Performed:**

Inquiries were made of management regarding internal controls to:

- Prevent fraud or abuse regarding Proposition K funds
- Ensure adequate separation of duties exists in the accounting for Proposition K funds
- Prevent material misstatements in the financial statements
- Ensure expenditures are allocated to the proper District funds

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 2011-12 financial statement balances for the Proposition K Bond Building Fund are not materially misstated.

**Results of Procedures Performed:**

The results of our audits 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.

<b>Facilities Site Walk</b>
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**Procedures Performed:**

We performed a site walk to verify that Proposition K funds expended for the fiscal year ended June 30, 2012 were for valid facilities acquisition and construction purposes. We toured the interim high school and the active construction site at the San Marcos High School reconstruction project. Through observation and inquiry, auditor was able to gain an understanding of the projects taking place and ensure that funds were being properly expended in accordance with the Proposition K ballot language.

**Results of Procedures Performed:**

Results of the site walks indicate that the major 2011-12 Proposition K construction activities at San Marcos High School were successfully completed and advanced into 2012-13 expenditure/construction phases where applicable.

## Tests of Expenditures

### **Procedures Performed:**

We tested expenditures to determine whether Proposition K Bond Building Fund funds were spent solely on voter and Board approved school facilities projects (as set forth in the District's Facilities Master Plan and the Proposition K ballot measure language). The expenditure test included a sample of 33 payments, totaling \$23.6 million, or approximately 65% of total expenditures for fiscal year 2011-12.

### **Results of Procedures Performed:**

We found the expenditures tested to be in compliance with the terms of the Proposition K Bond Building Fund ballot language, sound internal control practices, and applicable state laws and regulations without exception.

## Test of Contracts and Bid Procedures

### **Procedures Performed:**

For the fiscal year ended June 30, 2012, we performed testing of one lease-leaseback contract and two professional services contracts to determine that a formal, qualifications-based selection procedure was in place. The lease-leaseback contract was awarded to Lusardi Construction Company and the two professional services contracts were awarded to LPA Inc. and Ninyo & Moore, respectively. We determined in our testing whether proper selection procedures were followed for the contracts selected. We also performed testing of one change order which was charged to Proposition K during the 2011-12 fiscal year to determine the existence of supporting documentation and proper approvals, including governing board approval.

### **Results of Procedures Performed:**

We found that the contracts tested followed a formal, qualifications-based selection procedure, prior to being recommended to and awarded by the District's governing board. Per the results of our inquiry and testing, the selection procedure consisted of a five person panel using scorecards with points based on qualitative criteria to evaluate RFQ respondents based on submitted proposals and live interviews. The District employed Eric Hall & Associates to assist in coordinating, monitoring and reporting on the results of the selection procedure. In the case of the professional services contracts tested, the highest-scored vendor for each was recommended to the District's governing board by District staff. In the case of the lease-leaseback contract tested, the four highest-scored vendors were recommended to the District's governing board to receive "approved" status for prospective Proposition K construction projects. District staff then assigned one of the "approved" firms to the first project, recommending that the governing board approve Resolution #01-10/11 allowing Lusardi Construction Company to lease the San Marcos High School property.

We found that the change order awarded on the Lusardi contract for the San Marcos High School Reconstruction Project was accompanied by itemized supporting documentation and was reviewed and approved by three parties (contractor, architect and Director of Facilities) prior to being approved by the District's governing board.

The contracts and change order tested appear to be in compliance with District policies and procedures and Education Code requirements. However, in findings #2012-1 and #2012-2 we noted opportunities for improving internal controls over contractor selection and change order analysis.

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

In our opinion, the District complied, in all material respects, with the compliance requirements for the Proposition K Bond Building Fund, for the fiscal year ended June 30, 2012, as listed and tested above.

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.

This report is intended solely for the information and use of the District's Governing Board, the Proposition K Bond Building Fund Citizens' Bond Oversight Committee, management, others within the entity, and the taxpayers of San Marcos Unified School District and is not intended to be and should not be used by anyone other than these specified parties.

*Christy White Associates*

San Diego, California  
January 10, 2013



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## **FINDINGS AND RESPONSES SECTION**

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**PROPOSITION K BOND BUILDING FUND  
SAN MARCOS UNIFIED SCHOOL DISTRICT  
Schedule of Findings and Responses  
For the Fiscal Year Ended June 30, 2012**

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**FINDING #2012-1: CONTRACTOR SELECTION**

**Finding:** A formal, monitored and documented evaluation process was utilized in the selection of four “approved” contractors from a pool of RFQ respondents. The District utilizes an informal, undocumented process for the determination of which “approved” contractor will be chosen for a given project (such as the selection of Lusardi Construction Company for the San Marcos High School Reconstruction Project).

**Recommendation:** We recommend that the District document the qualifications-based selection decisions employed in the “approved” contractor selection process to better enhance the controls and transparency of the selection process.

**District Response:** In the future, District staff will document its contractor reviews, phone reference contacts and decision summarizations for audit transparency and documentation.

**FINDING #2012-2: CHANGE ORDER ANALYSIS**

**Finding:** Change orders are currently analyzed by a committee, including the contractor, architect and Director of Facilities, prior to approval from the District’s governing board. While this provides a good measure of consideration and oversight, the process could be further strengthened with the aid of a third party construction expert who could utilize detailed, industry standard metrics to analyze change order costs for accuracy and reasonableness. We note that as of December, 2012, the District has engaged with construction consulting firm fs3 Hodges to provide these services.

**Recommendation:** We concur with the District’s involvement of a third party construction expert to assist in analysis of change order accuracy and reasonableness.

**District Response:** As presented above, due to the large amount of DSA required changes to the current San Marcos High school construction project, the District hired a third party construction consultant in December 2012 to review the costs proposed for the associated change orders. This adds to the reviews conducted of the subcontractor’s costs by the General Contractor, Architect and Executive Director of Facilities.