

Primero Reorganized School District No. 2
Weston, Colorado

**PRIMERO RE-2 SCHOOL DISTRICT'S MANAGEMENT DISCUSSION AND
ANALYSIS OF FINANCIAL STANDING**

JUNE 30, 2007

The Governmental Accounting Standards Board issued an accounting standards statement in June 1999 that completely revised the financial information and the form of the financial statements that local governments are required to present under generally accepted accounting principles. For local governments of the size of the Primero RE-2 School District, the mandatory implementation date for the new requirements was the year ending June 30, 2004.

This is the District's management and discussion and analysis. It provides an overview of the District's financial activities for the fiscal year July 1, 2006 to June 30, 2007. Please read it in conjunction with the District's financial statements.

FINANCIAL HIGHLIGHTS

During the 2003-04 school year a completely new procedure was established to determine the District's net assets. The 2003-04 baseline data will be used to determine net increases/decreases for all future years.

Total net assets:

2006-07:	\$2,319,250.00
2005-06:	\$2,526,959.00 (-8.3%)
2004-05:	\$2,724,737.00 (+1%)
2003-04:	\$2,693,940.00 (baseline)

The General Fund reported a fund balance of \$688,193.00 at the close of the fiscal year 2007, which was lower than the previous year's \$914,434.00. The District strives to limit the spending of its reserves; however, unless other measures are initiated (such as voters passing a mill levy override) the District will eventually deplete its reserves in future years (see "Financial Analysis of the District as a Whole" below). Fortunately, District voters did approve two mill levy overrides in the November 2007 General Election (see below).

OVERVIEW OF THE FINANCIAL STATEMENTS

Management’s Discussion and Analysis is intended to serve as an introduction to the District’s basic financial statements. Comparison to the prior year’s activity is normally provided in this document. The School District’s basic financial statements are comprised of three components: (1) district-wide financial statements; (2) fund financial statements; and (3) notes to the basic financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

DISTRICT-WIDE FINANCIAL STATEMENTS

The District-wide Statements report information about the District as a whole using accounting methods similar to those used in private sector companies. The statement of net assets includes all of the governmental unit’s assets and liabilities.

The district-wide statements report the District’s net assets and how they have changed. Net assets, the difference between the District’s assets and liabilities, are one way to measure the District’s financial health or position. Increases or decreases in the District’s net assets could indicate whether the District’s financial health is improving or deteriorating. One needs to consider additional factors such as changes in the District’s tax base, changes in student enrollment and the condition of the school building.

Governmental activities: Most of the District’s basic services are included here, such as instruction, transportation, maintenance, operations and administration. State funding from equalization and property taxes finance most of these activities. This information is comprised of all of the Primero RE-2 School District Funds: General Fund, Preschool Fund, Capital Reserve Fund, Governmental Designated-Purpose Grants Fund, Pupil Activity Fund and the Food Services Fund.

Business-type activities: The District charges fees to help cover the costs of certain services it provides. This information is comprised from the Food Services Fund.

FUND FINANCIAL STATEMENTS

The Fund Financial Statements provide detailed information about the District’s funds, focusing on its most significant funds or “major” funds, not the District as a whole. Fund Financial Statements are designed to demonstrate compliance with finance-related legal requirements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The School District, like other governments, uses fund accounting to ensure and demonstrate compliance. All of the funds of the District can be divided into two categories: “governmental funds” and “proprietary funds.”

Governmental Funds: Most of the District’s basic services are reported in **governmental funds**, which generally focus on the determination of financial position and change in financial position, not on income determination. They are reported using an accounting method called “modified accrual accounting,” which measures cash and all other financial assets that can readily be

converted into cash. The governmental fund statements provide a detailed short-term view of the District's operations and the services it provides. Governmental fund information helps the reader determine whether there are more or fewer financial resources that can be spent in the near future to finance the District's programs. The relationship (or differences) between governmental activities (reported in the Statement of Net Assets and the Statement of Activities) and governmental funds is reconciled in the financial statements.

Proprietary Funds: Services for which the District charges a fee are generally reported in **proprietary funds**. Proprietary funds are reported in the same way as the district-wide statements. The district uses a proprietary fund to account for its food service operation.

NOTES TO THE FINANCIAL STATEMENTS

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

In addition to the financial statements and accompanying notes, this report also contains other supplemental information concerning the District's non-major governmental funds. The combined statements of the non-major governmental funds are presented after the notes to the financial statements.

FINANCIAL ANALYSIS OF THE DISTRICT AS A WHOLE

As noted earlier, net assets may serve, over time, as a useful indicator of the District's financial position. The District's total net assets on June 30, 2007 were \$2,319,250.00. Of the District's \$2,319,250.0 in assets, sixty-five percent (65%) -- \$1,496,080.00 -- reflects investment in capital assets (e.g., land, buildings, infrastructure, machinery and equipment). This is a decrease of \$207,709.00 in value over the \$2,526,959.00 in capital assets reported as of June 30, 2006.

The unrestricted net assets \$746,450.00 may be used to meet the District's ongoing financial obligations. Tabor Reserves amount to \$73,000, an increase of \$-0- over 2005-06. The District's unrestricted net assets decreased \$205,283 from 2005-06 to 2006-07.

The District's unrestricted net assets will eventually be depleted unless (a) pupil enrollment increases dramatically; (b) the district voters approve a mill levy override; and/or (c) the State increases funding levels for public schools. Currently, the unrestricted net assets permit the District to function without having to engage in short-term borrowing, therefore maintaining a proper cash flow between payments received from the State or County.

The Board of Education asked voters to consider approving a mill levy override in November 2006 for an additional \$300,000.00 per year. The ballot issue 3A was defeated by a narrow margin, 55% to 45%, therefore, the Board revised its plan and asked voters again to consider approving a mill levy override in November 2007. The Board approached voters with three ballot issues in November 2007, a \$10.7 million bond with a maximum 10 year repayment schedule, a \$350,000 per year general fund override, and a \$140,000 per year transportation fund override.

The District was very pleased that voters approved these three ballot issues in a nearly 2-1 margin of support. The additional override funds will help to hire, train and retain high-quality teachers; support elective course offerings, such as industrial arts and music; for alterations, improvements, equipment, furnishings, software and other long-range capital expenditures; additional technology resources; for staff training to improve instruction; and other necessary uses, including maintaining a stable unrestricted net asset account that will enable the District to have cash flows that will prevent short-term borrowing. The bond will permit the district to address significant health and safety issues in the current school facility, including a leaking roof, mold and asbestos abatement, and an aging septic system. A new wastewater treatment plant will be constructed, instead.

While the District's school facilities overall are in good condition, there are aspects of the facilities that must be improved, including replacing all exterior doors, replacing all glass with double pane safety glass, adding additional security and safety features to the physical plant and campus, adding an 11,000 square foot instructional space for industrial arts, art and music, updating the science lab, reconfiguring the main entrance of the school building, improving and increasing district housing for employees, and paving the athletic track. A community center will also be constructed onsite and the cafeteria expanded in size.

Where possible, appropriate and achievable, the District will also pursue future grant opportunities to increase funding available for instruction, special projects, and other initiatives. The district received \$250,000 of grants and donations in 2006-07 through the efforts of parents and staff to improve the playground, create a community use park, and upgrade the baseball field. The grants included a \$25,000 Gates Family Foundation Challenge Grant, a \$29,000 Department of Local Affairs Grant for the playground surface material, a \$153,000 Great Outdoors Colorado (GOCO) grant, and \$10,000 from Pioneer Natural Resources, the largest employer in the district.

Even with the voter-approved mill levy overrides, however, the District will not see these funds until the 2008-09 school year, so the expenditures for 2007-08 will be greatly reduced and must be extremely frugal. The budget for 2008-09 and years following must also be frugal because the District needs to rebuild both its operational and capital reserve funds.

As noted in our recent audit discussion with our auditor, the greatest area of expense for the district historically over the past ten years has been on staff. Unless staff had been laid off at the end of 2006-07 for the 2007-08 school year, there would have been no more room for budget reductions. Staffing will continue to be the largest source of expenditure in years to come.

Document prepared by Gerald W. Gabbard, Superintendent of Schools and Eric Davies, Business Manager

Primero RE-2 School District: Table 1—Assets, Liabilities & Net Assets 2007

KEY	Governmental Activities 2006-07	Governmental Activities 2005-06	Business-Type Activities 2006-07	Business-Type Activities 2005-06	Total 2006-07	Total 2005-06
ASSETS						
Current and other assets	\$976,756	\$1,165,579.00	\$10,156	\$2,433.00	\$988,978	\$1,168,012.00
Capital assets	\$3,780,288	\$3,642,695.00	\$42,147	\$42,147.00	\$3,822,435	\$3,684,862.00
Depreciation	(\$2,225,197)	(\$2,150,271.00)	(\$36,759)	(\$35,689.00)	(\$2,261,956)	(\$2,185,960.00)
Total Assets	\$2,533,913	\$2,658,003.00	\$15,544	\$8,891.00	\$2,549,457	\$2,666,894.00
% +/- of Total From Previous Year	-4.7%	-7.2%	+42.8%	-43.9%	-4.4%	-7.4%
Liabilities						
Current Liabilities	\$165,808	\$221,108.00	\$0.00	\$0.00	\$165,808	\$221,108.00
Long-term Liabilities	\$64,399	\$0.00	\$0.00	\$0.00	\$64,399	\$0.00
Total Liabilities	\$230,207	\$221,108.00	\$0.00	\$0.00	\$230,207	\$221,108.00
% +/- of Total From Previous Year	+3.95%	+43.3%	N/A	N/A	+3.95%	+43.3%

KEY	Governmental Activities 2006-07	Governmental Activities 2005-06	Business-Type Activities 2006-07	Business-Type Activities 2005-06	Total 2006-07	Total 2005-06
Net Assets						
Investment in Capital Assets, net of related debt	\$1,490,692	\$1,492,424.00	\$5,388	\$6,458.00	\$1,496,080	\$1,498,902.00
<i>Restricted for:</i>						
Tabor Reserve	\$73,000	\$70,800.00	N/A	N/A	\$73,000	\$70,800.00
Preschool	\$3,720				\$3,720	
Unrestricted Assets	\$736,294	\$948,361.00	\$10,156	\$8,916.00	\$746,450	\$957,277.00
Total Net Assets	\$2,303,706	\$2,511,585.00	\$15,544	\$15,374.00	\$2,319,250	\$2,526,959.00

Primero RE-2 School District: Table 2—Changes in Net Assets 2006 to 2007

Key	Governmental Activities 2006-2007	Governmental Activities 2005-2006	Business-Type Activities 2006-2007	Business-Type Activities 2005-2006	Total 2006-2007	Total 2005-2006
<i>Program Revenues:</i>						
Charges for Services	\$97,095	\$55,553.00	\$9,288	\$10,426.00	\$106,383	\$65,979.00
Operating Grants & Contributions	\$120,856	\$130,693.00	\$39,039	\$40,291.00	\$159,895	\$170,984.00
Capital Grants & Contributions	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
Operations & Transportation	\$46,077	\$44,663.00	\$0.00	\$0.00	\$46,077	\$44,663.00
<i>General Revenues:</i>						
Property Taxes	\$791,557	\$780,716.00	\$0.00	\$0.00	\$791,557	\$780,716.00
Specific Ownership Taxes	\$163,496	\$165,365.00	\$0.00	\$0.00	\$163,496	\$165,365.00
State Equalization	\$1,189,325	\$1,115,654.00	\$0.00	\$0.00	\$1,189,325	\$1,115,654.00
Earnings on Investments	\$7,138	\$7,828.00	\$43.00	\$35.00	\$7,138	\$7,863.00
Other Revenues	\$11,097	\$61,864.00	\$0.00	\$0.00	\$11,097	\$61,864.00
Transfers	(\$81,000)	(\$70,000.00)	\$81,000	\$70,000.00	(\$81,000)	(\$0.00)
Total Revenues	\$2,345,641	\$2,292,336.00	\$129,370	\$120,752.00	\$2,475,011	\$2,413,088.00
Expenses						
Instructional Services	\$1,388,493	\$1,423,573.00	\$0.00	\$0.00	\$1,388,493	\$1,423,573.00
<i>Supporting Services:</i>						
Students	\$136,188	\$61,863.00	\$0.00	\$0.00	\$136,188	\$61,863.00
Instructional Staff	\$32,624	\$21,977.00	\$0.00	\$0.00	\$32,624	\$21,977.00
District Administration	\$219,104	\$205,815.00	\$0.00	\$0.00	\$219,104	\$205,815.00
School Administration	\$71,612	\$76,702.00	\$0.00	\$0.00	\$71,612	\$76,702.00
Business	\$61,928	\$64,297.00	\$0.00	\$0.00	\$61,928	\$64,297.00
Operations & Maintenance	\$356,942	\$322,241.00	\$0.00	\$0.00	\$356,942	\$322,241.00
Transportation	\$214,153	\$243,370.00	\$0.00	\$0.00	\$214,153	\$243,370.00
Central	\$65,470	\$56,799.00	\$0.00	\$0.00	\$65,470	\$56,799.00
Insurance	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00	\$0.00
Capital Outlay	\$4,079	\$12,998.00	\$0.00	\$0.00	\$4,079	\$12,998.00
Interest on Long-term Liabilities	\$2,927	\$0.00	\$0.00	\$0.00	\$2,927	\$0.00
Food Service	\$0.00	\$0.00	\$129,200	\$121,211.00	\$129,200	\$121,211.00
Total Expenses	\$2,553,520	\$2,512,823.00	\$129,200	\$121,211.00	\$2,682,720	\$2,634,034.00

Increase/Decrease in Net Assets	(\$207,879)	(\$220,487.00)	\$170	(\$459.00)	(\$207,709)	(\$220,946.00)
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The District's total revenue

was **\$2,475,011**. A significant portion, 49.97%, of the revenue comes from state equalization. Property taxes account for 30.97% of the District's revenue and the remaining 19.06% comes from other federal, state and local sources. The total cost of all governmental activities was \$2,553,520.00. The bulk of these expenses, \$1,703,586.00, or 69.9%, was allocated for instruction and support services (not including operations and maintenance, transportation, and capital outlay.) When expenditures exceed revenues for a fiscal year, as they did again in 2006-07, as they did in 2005-06, the District was forced to spend its reserves, resulting in a decline in net assets. The District's operational reserves have been declining steadily for the past five years. This is mainly due to increased staffing without additional revenue to offset the cost of the additional staff. The only way the District would significantly reduce expenditures without other external sources of revenue would be to lay-off staff. This was not a goal of the District's Board of Education, however; thus, the deficit spending of operational reserves has continued into the 2006-07 fiscal year.

The District has explored alternate ways to increase revenues, such as those outlined in the Management Discussion and Analysis above, including convincing voters of the needs to pass a bond and a general fund and transportation fund override.

GOVERNMENTAL ACTIVITIES

The table below illustrates the total cost of the District's major services. It also shows the net costs of these services. The net cost includes all expenses for the particular service, less any revenue for the service.

Primero RE-2 School District: TABLE 3—Activities 2006 to 2007

Key	Total Cost of Services 2006-07	Total Cost of Services 2005-06	Net Cost of Services 2006-07	Net Cost of Services 2005-06
Instructional Services	\$1,388,493	\$1,423,573.00	\$1,267,637	\$1,423,573.00
<i>Supporting Services</i>				
Students	\$136,188	\$61,863.00	\$53,124	\$61,863.00
Instructional Staff	\$32,624	\$21,977.00	\$32,624	\$21,977.00
District Administration	\$219,104	\$205,815.00	\$219,104	\$205,815.00
School Administration	\$71,612	\$76,702.00	\$71,612	\$76,702.00
Business	\$61,928	\$64,297.00	\$61,928	\$64,297.00
Operation & Maintenance	\$356,942	\$322,241.00	\$342,911	\$322,241.00
Transportation	\$214,153	\$243,370.00	\$168,076	\$198,707.00
Central	\$65,470	\$56,799.00	\$65,470	\$56,799.00
Insurance	\$0.00	\$0.00	\$0.00	\$0.00
Capital Outlay	\$4,079	\$12,998.00	\$4,079	(\$12,998.00)
Interest on Long-term Liabilities	\$2,927	\$0.00	\$2,927	\$0.00
Food Service	\$129,200	\$121,211.00	\$80,873	\$121,211.00
Total	\$2,682,720	\$2,512,823.00	\$2,370,365	\$2,217,946.00

BUSINESS-TYPE ACTIVITIES

Business-type activities are made up of the Food Service Fund. This program had revenues of \$48,327.00 and expenses of \$129,200.00. The District's hot lunch/breakfast program is a recipient of Federal food commodities and is impacted when these commodities are not available to the District. The Food Service Fund was subsidized with \$81,000.00 from the General Fund. The District plans to increase lunch costs to regular paying student and adult customers in 2006-07 to generate slightly more revenue. The milk price for extra cartons was set at \$0.50 each in 2006-07.

FINANCIAL ANALYSIS OF THE DISTRICT'S FUNDS

State equalization for the General Fund and the Colorado Preschool Project Fund is based on pupil count. State equalization funding, the per pupil amount set by the Colorado Department of Education, along with local property tax and specific ownership taxes, decreased due to a decrease in the number of pupils in the district this year. Those students enrolled in preschool who qualify for the Colorado Preschool Project program and those students enrolled in full-day Kindergarten are funded at three-eighths (0.375) and one-half (0.50) of the per pupil rate, respectively, of all other students enrolled in the District, who are funded at 100% of the per pupil rate of approximately \$9,800.00. There were 210.5 FTE students enrolled in the Primero RE-2 School District on October 1, 2006.

GENERAL FUND BUDGETARY HIGH-LIGHTS

Over the course of the year, the District amended its budget. Actual expenditures of \$2,682,720.00 continued to be higher than expected, as they were in 2005-06. Unfortunately, actual revenues of \$2,426,641.00 were only slightly above the budgeted amount, so the increase did not help dramatically increase the operational reserves the District needs to maintain a cash flow cushion for the times between when it receives its State and County payments. The District continues to maintain frugal spending habits in an effort to spend only the money that is collected in a year, however, due to decreased enrollment over the past few years, increased expenses, and limited resources, the District had to dip into its operational reserves for an additional \$226,241.00 in fiscal year 2006-07. Combined with the use of reserves in 2005-06 of \$220,487.00, this accounts for a depletion in operational reserves over a 2 year fiscal period of \$446,728.00.

The Board decided in February 2007 to approach voters again regarding a mill levy override and also a bond issue. The Board placed 3 ballot issues on the November 2007 general election, including a \$350,000 per year general fund mill levy override, a \$140,000 per year transportation fund mill levy override, and a \$10.7 million bond issue. Fortunately, these issues passed on a 2-1 margin by voters, however, the mill levy funds will not impact the budget until the 2008-2009 fiscal year. The District sold bonds in December 2007 and received these funds on December 19, 2007, which will only impact the design and construction of building improvements, upgrades, renovations and additions. The mill levy overrides will be reflected in the 2008-2009 budget and audit, and the bond will be seen starting in the 2007-2008 budget and audit.

CAPITAL ASSETS AND DEBT ADMINISTRATION

The District's investment in capital assets for its governmental activities as of June 30, 2007 amounts to \$1,555,091.00. The next table outlines the District's capital assets, net of depreciation.

Primero RE-2 School District: Table 4—Capital Assets 2006-2007 (Net of Depreciation)

Key	Capital Assets June 30, 2007	Capital Assets June 30, 2006
Land and Sites	\$128,893	\$128,893.00
Buildings	\$1,203,774	\$1,194,119.00
Vehicles	\$107,663	\$128,477.00
Equipment	\$114,761	\$40,935.00
Total Capital Assets	\$1,555,091	\$1,492,424.00

LONG-TERM DEBT

The Primero RE-2 School District currently has a limited amount of long-term debt from a fluorescent lighting lease. New lights were installed in the district in the summer of 2006 for \$73,462.00. The lease repayment schedule is for 5 years. The district's principal payments in 2006-07 amounted to \$9,063 and interest payments accounted for \$1,708.00. Since voters approved a \$10.7 million bond in November 2007, the debt service from this referendum will begin to impact the District's budget and audits in the 2008-2009 fiscal year.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The budget for the 2007-08 school year will, as always, be impacted by student enrollment. The District was very pleased that enrollment as of October 1, 2007 reached 215.5 FTEs. The District had been in a slowly declining enrollment phase in the previous two years 2004-05 and 2005-06, but enrollment in 2006-07 began to stabilize at 210.5 FTEs as of the October 1, 2006 count day. The District's enrollment is subject to the unpredictable employment situation of the highly volatile natural gas and oil industry in the region. The District's property taxes have been impacted by the exploding gas industry as the assessed valuation of the District has increased from about \$51,000,000 in 2000 to a high of just over \$424 million in 2006. It dropped back to \$374 million in 2007. Primero's mill levy is the lowest in the State of Colorado for 2007 at 1.8 mills.

Increased health insurance, utility and fuel costs and the rising percentage the District contributes to PERA all increase the problem of keeping spending in line with anticipated revenues. The State of Colorado forecasted in September 2006 that inflation rates would decrease from 3.3% to 3.1, thus impacting the revenue schools can expect to receive from Amendment 23. TABOR continues to require that the District reserve \$70,000 per year or more. The District allocated \$73,000 for TABOR in 2006-07. The District's budget for 2007-08 is a very conservative one with little room for flexibility unless a mill levy override is approved by voters. The District was

able to reduce \$380,000 of spending for 2007-08 without having to lay off staff, however, there is no more room for cuts without affecting staffing levels. Despite the fact that voters passed two mill levy overrides totaling up to \$500,00 additional funds per year for the operational budget, these monies will not be seen until at least June 2007, thus, not impacting the District's budget until the 2008-2009 school year.

Primero RE-2 is committed to keeping the base salary for certified and classified employees at a level equal to or above other districts in Las Animas County, if at all possible, in order to attract and retain quality instructors and support staff. The District's goal is to monitor spending in the District and to eliminate in future years expending more than the District receives in revenue. All staff agreed to a pay raise freeze in 2007-08 to assist with the budget problem. Staff only received steps and years of experience increases, not a percentage increase on the base salaries.

The District's Board of Education is in the process of analyzing program needs to the next three to five years and will prepare both an annual and long-term budget for 2008-2009 and 2008-2012.

Primero is caught in a no-win situation with the state's funding formula and an unreasonable increase from the State for subsequent years

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT TEAM

This financial report is designed to provide taxpayers, customers, prospective students and parents, and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the monies it receives and expends. The District's Board, Administration and Staff understand that the reader's questions may not have been entirely answered by reviewing this report; therefore, the reader is invited to contact the following personnel at the Primero RE-2 School District office for further information:

Primero RE-2 School District

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