

MANAGEMENT'S DISCUSSION AND ANALYSIS

Our discussion and analysis of the Kent School District's financial performance provides an overview of the district's financial activities for the fiscal year ended August 31, 2006. We encourage readers to consider the information presented here in conjunction with additional information that we have furnished in our letter of transmittal, which can be found on pages 1-7 of this report.

FINANCIAL HIGHLIGHTS

- The district's total net assets of governmental activities as of August 31, 2006, were \$240 million, an increase of \$22 million. This increase is attributable to the increase in overall revenues and lower payments of interest due to the issuance of the 2005 advance refunding bonds.
- During the year, the district had revenues of \$244 million and expenses of \$221 million incurred for all governmental activities, resulting in a corresponding increase in the district's net assets by \$22 million.
- As of the close of the current fiscal year, the Kent School District's governmental funds reported combined ending fund balances of \$50 million, a decrease of \$1 million in comparison with the prior year. Approximately \$23 million is available for spending at the district's discretion (unreserved, undesignated fund balance).
- At the end of the current fiscal year, unreserved, undesignated fund balance for the general fund was \$12 million, or 6.24 percent of total general fund expenditures.
- The Kent School District's total debt decreased by \$15 million during the current fiscal year. This decrease was due the fact that the district did not issue any new debt during the 05-06 fiscal year.

OVERVIEW OF THE FINANCIAL STATEMENTS

The Kent School District's financial statements consist of three components:

1) government-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.

The basic financial statements include two kinds of statements that present different views of the district:

- The first two statements (*statement of net assets* and *statement of activities*) are *district-wide financial statements* that provide both short-term and long-term information about the district's *overall* financial status as a *whole*.
- The *governmental fund financial statements* that focus on *individual* parts of the district, report the district's operations in more detail than the district-wide statements. These *governmental fund statements* tell how basic services such as regular and special education were financed in the short term as well as what remains for future spending.
- The remaining statements provide financial information about activities for which the district acts solely as a trustee for the benefit of those outside of the district.

The financial statements also include notes that explain some of the information in the statements and provide more detailed data. The statements are followed by a section of required

supplementary information that further explains and supports the financial statements with a comparison of fund activity to the district's budget for the year.

Government-Wide Financial Statements. The *government-wide financial statements* are designed to provide readers with a broad overview of the Kent School District's finances, in a manner similar to private-sector business.

The *Statement of Net Assets* presents information about the district as a whole and about its assets and liabilities, with the difference between the two reported as *net assets*. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the district is improving or deteriorating. This statement uses the accrual basis of accounting, which is similar to the accounting used by most private-sector companies.

The *Statement of Activities* presents information showing how the district's net assets changed during the current fiscal year. All of the current year's revenues and expenses are reported, *regardless of the timing of related cash flows*.

In the *Statement of Net Assets* and *Statement of Activities*, most of the district's basic services are reported in governmental activities, including general fund, associated student body, debt service, capital projects, transportation vehicle, and permanent funds.

Governmental Fund Financial Statements. Governmental fund financial statements provide detailed information about the most significant funds - not the district as a whole. These funds are required to be established by Washington State law. These statements focus on *near-term inflows and outflows of spendable resources*, as well as on *balances of spendable resources* available at the end of the fiscal year.

These funds are reported using the modified accrual basis of accounting, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the district's general education and support operations and the basic services it provides. Governmental fund information helps determine whether there are more or fewer financial resources that can be spent in the near future to finance the district's programs. We describe the relationship (or differences) between governmental activities (reported in the *Statement of Net Assets* and the *Statement of Activities*) and governmental funds in two reconciliations (Schedules 3A and 4A) in the basic financial statements, and in Note 9 to Financial Statements.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

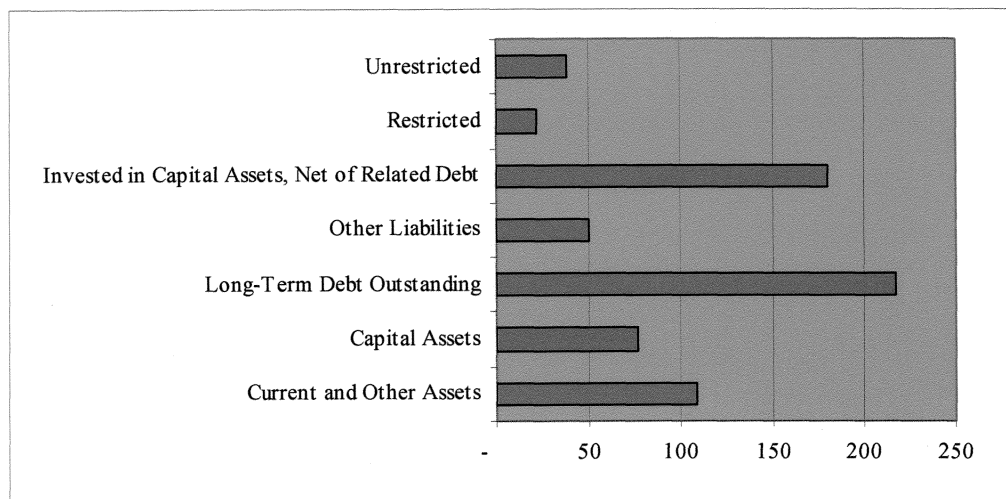
Net assets may serve as a useful indicator of a government's financial position. The Kent School District's assets exceeded liabilities by \$240 million at the end of the 2005-06 fiscal year.

The largest portion of net assets is invested in capital assets. The investment in capital assets (e.g., land, building, and equipment), less any related outstanding debt used to acquire those assets, is currently \$180 million. The remainder consists of amounts restricted for capital projects, debt service, and other purposes, with \$39 million unrestricted. The district's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

NET ASSETS

	Primary Government Governmental Activities		
	Aug 31, 2006	Aug 31, 2005	Changes
ASSETS			
Current and Other Assets	\$ 108,201,541	\$ 99,813,995	\$ 8,387,546
Capital Assets	322,684,462	394,452,728	(71,768,267)
Deferred Charges/Prepays	76,908,253	2,114,687	74,793,566
Total Assets	507,794,256	496,381,410	11,412,845
LIABILITIES			
Long-Term Debt Outstanding	216,602,140	232,018,417	(15,416,277)
Other Liabilities	50,708,020	45,884,192	4,823,827
Total Liabilities	267,310,160	277,902,609	(10,592,450)
NET ASSETS			
Invested in Capital Assets, Net of Related Debt	179,939,017	158,676,022	21,262,995
Restricted	21,776,982	27,307,463	(5,530,481)
Unrestricted	38,768,096	32,495,308	6,272,788
TOTAL NET ASSETS	\$ 240,484,095	\$ 218,478,793	\$ 22,005,302

Net Assets Chart (in Millions)



KENT SCHOOL DISTRICT NO. 415, Management's Discussion and Analysis, Continued

The restricted net assets represent resources that are subject to external restrictions on how they may be used. The remaining balance of unrestricted *net assets* may be used to meet the district's ongoing obligations to citizens and creditors.

Governmental Activities. Governmental activities improved the district's overall financial position, increasing the district's net assets by \$22 million. This is the district's fifth year of reporting a *Statement of Activities* under the new GASB Statement 34 reporting requirements for school districts in the State of Washington.

Changes in Net Assets			
Primary Government			
Governmental Activities			
	2005-06	2004-05	Changes
REVENUES			
Program Revenues:			
Charges for Services	\$ 16,279,867	\$ 10,126,452	\$ 6,153,415
Operating Grants and Contributions	44,311,179	41,124,147	3,187,032
Capital Grants and Contributions	9,607	124,937	(115,330)
General Revenues:			
Property Taxes	68,490,888	66,134,593	2,356,295
Interest and Investment Earnings	2,285,572	1,369,690	915,882
Unallocated Revenues	112,131,486	121,389,964	(9,258,478)
TOTAL REVENUES	243,508,599	240,269,783	3,238,816
PROGRAM EXPENSES:			
Regular Instruction	122,400,076	117,610,800	4,789,276
Special Instruction	19,221,145	19,539,615	(318,470)
Vocational & Skill Center Instruction	5,864,704	5,910,315	(45,611)
Compensatory Instruction	17,855,063	17,217,807	637,256
Other Instr. & Community Services	886,534	1,124,433	(237,899)
Support Services	41,626,199	41,612,199	14,000
Extracurricular Activities	3,122,145	2,923,943	198,202
Debt Interest Payment	10,049,805	9,870,549	179,256
Payment to Refunded Escrow	96,193	4,378,855	(4,282,662)
TOTAL EXPENSES	221,121,863	220,188,515	933,349
INCREASE (DECREASE) IN NET ASSETS	22,386,736	20,081,268	2,305,467
BEGINNING NET ASSETS	218,478,794	198,397,526	20,081,268
Prior Year Adjustments	(381,435)	-	(381,435)
Net Assets, Restated	218,097,359	198,397,526	19,699,833
ENDING NET ASSETS	\$ 240,484,095	\$ 218,478,794	\$ 22,005,301

The following table presents the cost of each of the district's largest programs – regular instruction, special instruction, vocational instruction, compensatory instruction, other instructional programs, and support services – as well as each program's net costs (total cost less revenues generated by the activities). The net cost column shows the financial impact by each of these functions.

	Governmental Activities			
	Total Costs of Services		Net Costs of Services	
	2005-06	2004-05	2005-06	2004-05
Regular Instruction	\$ 122,400,076	\$ 117,610,800	\$ (117,018,144)	\$ (116,039,675)
Special Instruction	19,221,145	19,539,615	(1,492,365)	(3,273,832)
Vocational Instruction	5,864,704	5,910,315	(5,560,931)	(5,624,352)
Compensatory Instruction	17,855,063	17,217,807	(1,721)	(1,162,920)
Other Instructional Programs	565,995	820,811	(146,833)	(251,595)
Community Services	320,539	303,622	(190,368)	(303,622)
Support Services	41,626,199	41,612,199	(26,012,616)	(27,795,273)
Extracurricular Activities	3,122,145	2,923,943	47,766	(112,307)
Other	96,193	4,378,855	(96,193)	(4,378,855)
Debt Payments	10,049,805	9,870,549	(10,049,805)	(9,870,549)
TOTALS	\$ 221,121,863	\$ 220,188,515	\$ (160,521,210)	\$ (168,812,979)

GOVERNMENTAL FUNDS FINANCIAL ANALYSIS

The focus of the district's *governmental funds* is to provide information on near-term inflows, outflows, and balances of *spendable resources*. Thus, unreserved fund balance may serve as a useful measure of the district's net resources available for spending at the end of the fiscal year.

As the district completed the fiscal year, its governmental funds (as presented in the balance sheets in the Governmental Fund Financial Statement section) reported a combined fund balance of \$50 million, which is \$.92 million lower than last year. This change is the result of the following factors:

- The fund balance in the General Fund increased by \$6.9 million, because the local property taxes were higher, state and federal funds were also higher, along with district efforts to cut costs.
- The fund balance in the Special Revenue (ASB) Fund remained almost the same.
- The fund balance in the Debt Service Fund decreased by \$.33 million. The district traditionally sets the property tax levy to closely match scheduled bond payments in order to moderate the impact of local property taxes.
- The fund balance in the Capital Projects Fund decreased by \$7.45 million due to increased expenditures for the construction of numerous capital projects.
- The fund balance in the Transportation Vehicle Fund decreased by \$.06 million, reflecting the costs of new buses that were higher than the replacement funding received from the state.
- The Permanent Fund (Reeploeg Trust) had no significant change on fund balance.

The following table presents a summary of the governmental funds' revenues and expenditures for 2005-06, and the amounts and percentages of increases and decreases in relation to the prior year.

Changes in Revenues and Expenditures				
Governmental Funds				
	2005-06	Percent of	Increase	Percent
	Amount	Total	(Decrease)	Increase
Revenue Source				
Local Taxes & Non-Tax	\$ 77,738,720	32.0%	\$ 3,293,101	4.42%
State Revenues	146,182,364	60.2%	323,577	0.22%
Federal Revenues	15,393,055	6.3%	520,310	3.50%
Other Revenues	3,388,136	1.4%	211,896	6.67%
Total Revenues	242,702,274	100.0%	4,348,884	1.82%
Expenditures				
Regular Instruction	112,289,776	46.2%	2,533,334	2.31%
Special Instruction	19,000,317	7.8%	765,609	4.20%
Vocational Instruction	5,720,195	2.4%	204,587	3.71%
Compensatory Instruction	17,649,844	7.3%	1,581,887	9.84%
Other Instruction Programs	549,742	0.2%	(216,253)	-28.23%
Community Services	316,914	0.1%	33,569	11.85%
Support Services	39,899,749	16.4%	1,954,980	5.15%
Student Activities	3,116,621	1.3%	192,678	6.59%
Capital Outlay	18,097,381	7.4%	(18,132,448)	-50.05%
Debt Service	26,621,687	10.9%	4,638,082	21.10%
Total Expenditures	243,262,226	100.0%	(6,443,976)	-2.58%
Other Financing Sources	19,504		(101,378,567)	-99.98%
Other Financing Uses	\$ -		\$ 75,578,855	-100.00%

General Fund Budgetary Highlights

Appropriations are a prerequisite to expenditures in the governmental funds. Appropriations lapse at the end of the fiscal year. The Board may adopt a revised or supplemental budget appropriation after a public hearing anytime during the fiscal year. There were no budget revisions in the general fund during 2005-06.

The general fund balance reported on Schedule A-1, on August 31, 2006, differs from the budgetary fund balance by \$21 million. The beginning fund balance was higher than budgeted by \$1.8 million, revenues were lower than budgeted by \$.62 million, and expenditures were lower than budgeted by \$19.71 million. Washington statutes establish expenditure budgets as absolute expenditure limits, encouraging contingency budgeting.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

At the end of the fiscal year 2005-06, the district had \$523 million invested in a broad range of capital assets, including school buildings, buses, and equipment.

**Capital Assets at Year-End
Governmental Activities
(in millions)**

	Historical Cost	Accumulated Depreciation	Net
Land	\$ 62.03	\$ -	\$ 62.03
Buildings & Improvements	364.18	107.66	256.52
Equipment	20.24	14.69	5.55
Construction-in-progress	76.28	-	76.28
	\$ 522.73	\$ 122.36	\$ 400.37

The district does not own general-purpose infrastructure assets (roads, bridges, tunnels, drainage systems, water and sewer systems, dams, lighting systems).

More information on the district's capital assets can be found in Note 4 in the Notes to the Financial Statements.

Long-Term Debt

At year-end, the district had \$220,201,842 in refunding, limited and unlimited tax general obligation bonds outstanding versus \$235,345,839 last year; a decrease of 6.43% as shown below:

**Outstanding Debt at Year-End
(in millions)**

	2005-2006	2004-2005	Increase(Decrease)	
1992A Refunding	\$ 9.595	\$ 11.650	\$ (2.06)	-17.6%
1992C Building Fund	4.555	4.555	-	0.0%
1993A Refunding	10.760	12.325	(1.57)	-12.7%
1993B Refunding	5.140	5.140	-	0.0%
1994 Building Fund	2.655	2.655	-	0.0%
1996 Building Fund	1.520	2.950	(1.43)	-48.5%
1997 Building & Ref.	17.600	20.105	(2.51)	-12.5%
1998 Building Fund	3.820	3.820	-	0.0%
2001A Building Fund	3.610	5.765	(2.16)	-37.4%
2001B Building Fund	17.965	17.965	-	0.0%
2002 Building & Ref.	28.250	30.520	(2.27)	-7.4%
2003 Building Fund	23.030	24.020	(0.99)	-4.1%
2004 Building Fund	23.500	24.500	(1.00)	-4.1%
2005 Refunding	68.100	69.265	(1.17)	-1.7%
2005 LGO Bonds	0.102	0.111	(0.01)	-8.3%
TOTALS	\$ 220.202	\$ 235.346	\$ (15.14)	-6.43%

Outstanding debt will mature on the following dates:

1992A Refunding	December 1, 2009
1992C Building Fund	December 1, 2008
1993A Refunding	December 1, 2011
1993B Refunding	December 1, 2008
1994 Building Fund	June 1, 2008

1997 Building & Refunding	December 1, 2016
1998 Building Fund	December 1, 2018
2001A Building Fund	December 1, 2007
2001B Building Fund	June 1, 2016
2002 Building & Refunding	December 1, 2022
2003 Building Fund	December 1, 2022
2004 Building Fund	December 1, 2024
2005 Refunding	December 1, 2018
2005 LGO Bonds	January 1, 2015

The district's most recent underlying bond ratings were as follows:

Moody's: Aa3 Standard and Poor's: AA-

The state limits the amount of general obligation debts (non-voted) that the district can issue to .375% of the assessed valuation of all taxable property within the district. This amount is calculated to be \$83,766,933. The limits for voted debts are 5.0 % of the assessed valuation of all taxable property within the district, provided the indebtedness in excess of 2.5% is for capital outlay, and an approval rate of 60% of the people who voted. This district limit is \$701,214,193.

More information on the district's debt can be found in Note 7 in the notes to the financial statements.

ECONOMIC FACTORS

Kent School District is located in south King County and the district is the fourth largest in the state of Washington. The district, with approximately 26,000 students, covers 73 square miles of area, with a population of approximately 144,000. The district serves the cities of Kent and Covington, and borders on or serves parts of the cities of Renton, Sea-Tac, Federal Way, Auburn, Black Diamond and Maple Valley.

The economy of the area is comprised of manufacturing, freight transfer, and retail services. The district's assessed valuation has grown by 89% since 1997. The top ten taxpayers comprise about 2.03% of the district's overall tax base. The Boeing Corporation is the largest of these, with the others representing manufacturing, utilities, communications, and aerospace.

The Washington State's fund balances in general fund were projected, in June 2006 in its six-year outlook, to end with positive fund balances from 2006 through 2011. The K-12 teacher/staff cost of living adjustments provided under state Initiative 732 to be \$143 million in 2008, \$201 million in 2009, \$302 million in 2010, and \$399 million in 2011.

Washington per capita personal income was down from \$36,045 in 2004 to \$35,409 in 2005. The wage and salary employment rose from \$2,913,395 in 2003 to \$2,957,913 in 2004. The unemployment rate was down from 6.5% in 2004 to 5.5% in 2005.

NEXT YEAR'S APPROPRIATIONS AND BUDGET RATES

The 2006-07 appropriations for governmental funds of the district were set at \$300 million, up by 9.5% from total appropriations of \$274 million last year.

Property tax rates of \$4.52 per \$1,000 were budgeted for 2007, a decrease of 1.52% from the 2006 actual tax rates of \$4.59.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the district's finances, and to show the district's accountability for the money it receives. If you have questions about this report, or would like additional financial information, contact the district's Finance Department at 12033 SE 256th Street, A-600, Kent, Washington 98030-6643.