



**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

REGULAR AUDIT

FOR THE YEAR ENDED JUNE 30, 2005



**Auditor of State
Betty Montgomery**

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

TABLE OF CONTENTS

TITLE	PAGE
Independent Accountants' Report.....	1
Management's Discussion and Analysis.....	3
Statement of Net Assets as of June 30, 2005.....	7
Statement of Revenues, Expenses, and Changes in Net Assets For the Fiscal Year Ended June 30, 2005	8
Statement of Cash Flows For the Fiscal Year Ended June 30, 2005	9
Notes to the Basic Financial Statements	11
Independent Accountants' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Required by <i>Government Auditing Standards</i>	21

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Auditor of State Betty Montgomery

INDEPENDENT ACCOUNTANTS' REPORT

ScholARTS Preparatory Middle School
Franklin County
400 E. Town Street
Columbus, Ohio 43215

To the Board of Directors:

We have audited the accompanying basic financial statements of the ScholARTS Preparatory Middle School, Franklin County, Ohio (the School), as of and for the year ended June 30, 2005 as listed in the table of contents. These financial statements are the responsibility of the School'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 the Comptroller General of the United States' *Government Auditing Standards*. Those standards require that we plan and perform the audit to reasonably assure 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 our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of ScholARTS Preparatory Middle School, Franklin County, Ohio, as of June 30, 2005, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The School is experiencing certain financial difficulties. Those difficulties and management's plan are discussed in Note 16.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 27, 2006, on our consideration of the School's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. While we did not opine on the internal control over financial reporting or on compliance, that report describes the scope of our testing of internal control over financial reporting and compliance and the results of that testing. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*. You should read it in conjunction with this report in assessing the results of our audit.

Management's Discussion & Analysis is not a required part of the basic financial statements but is supplementary information the Governmental Accounting Standards Board requires. We have applied certain limited procedures, consisting principally of inquiries of management regarding the methods of measuring and presenting the required supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in black ink that reads "Betty Montgomery". The signature is written in a cursive, flowing style.

Betty Montgomery
Auditor of State

February 27, 2006

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2005
UNAUDITED**

The discussion and analysis of the ScholARTS Preparatory Middle School's (the School) financial performance provides an overall view of the School's financial activities for the fiscal year ended June 30, 2005. The intent of this discussion and analysis is to look at the School's financial performance as a whole; readers should also review the notes to the basic financial statements and basic financial statements to enhance their understanding of the School's financial performance. This was the first full fiscal year of operations.

Financial Highlights

- Total Assets were \$56,160. The total assets of the School consisted of cash on hand, prepaid items, state and federal grants receivable, and capital assets.
- Total Liabilities were \$83,279. The liabilities at year end are attributable to personal related and material and supply costs that were earned prior to June 30, 2005, but were not paid until after June 30, 2005. Payroll and benefits are provided throughout the year based on employees service during the year. The School will receive state foundation revenue during the summer months to meet these obligations as they become due.
- Total Net Assets were negative \$27,119. The 2004-2005 school year was the first year the school provided instructional services to students and therefore, fiscal year 2005 was the first year the school received revenues from the state foundation program.
- Total Change in Net Assets was negative \$32,839.

Using this Annual Financial Report

This financial report consists of three parts, the Management's Discussion and Analysis (MD&A), the basic financial statements, and notes to those statements. The basic financial statements include a statement of net assets, a statement of revenues, expenses and changes in net assets, and statement of cash flows. As the School reports its operations using enterprise fund accounting, all financial transactions and accounts are reported as one activity, therefore the entity wide and the fund presentations information is the same.

Statement of Net Assets

The Statement of Net Assets answers the question, "How did we do financially during 2005?" This statement includes all assets and liabilities, both financial and capital, and short-term and long-term using the accrual basis of accounting and economic resources focus, which is similar to the accounting used by most private-sector companies. This basis of accounting considers all of the current year's revenues and expenses regardless of when cash is received or paid.

The School has presented for the first time basic financial statements. See Note 2- H. Although the School's first required audited financial statement period was for the year ended June 30, 2005, limited activity prior to July 1, 2004, has been restated and is presented for comparison purposes in this discussion and analysis.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2005
UNAUDITED
(Continued)**

Table 1 provides a summary of the School's net assets for fiscal year 2005 compared to fiscal year 2004:

Table 1 Net Assets		
	2005	2004
Assets		
Current Assets	\$ 20,992	\$ 4,851
Security Deposit	7,917	-
Capital Assets, Net	27,251	3,324
Total Assets	\$ 56,160	\$ 8,175
Liabilities		
Current Liabilities	\$ 83,279	\$ 2,455
Net Assets		
Invested in Capital Assets	27,251	3,324
Restricted	885	2,373
Unrestricted	(55,255)	23
Total Net Assets	\$ (27,119)	\$ 5,720

Total assets increased by \$47,985. While cash and cash equivalents increased by \$9,689, total receivables increased by \$4,902. Total liabilities increased by \$80,824. The School's net assets decreased by \$32,839. This was the first full fiscal year of operations.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2005
UNAUDITED
(Continued)**

Table 2 shows the changes in net assets for fiscal year 2005 as compared to fiscal year 2004.

Table 2
Change in Net Assets

	2005	2004
Revenues		
Operating Revenues:		
Foundation Payments	\$ 278,576	\$ -
Disadvantaged Pupil Impact Aid	9,790	-
Special Education	5,724	-
Food Services	180	-
Other Operating Revenues	1,639	-
Non-Operating Revenues:		
Federal and State Grants	157,523	50,000
Contributions and Donations	561	-
Interest	22	23
Total Revenues	454,015	50,023
Expenses		
Operating Expenses		
Salaries	149,300	-
Fringe Benefits	35,021	-
Purchased Services	203,575	43,111
Materials and Supplies	77,672	361
Depreciation	7,020	831
Other Expenses	13,761	-
Non-Operating Expenses:		
Other Expenses	505	-
Total Expenses	486,854	44,303
Increase/(Decrease) in Net Assets	\$ (32,839)	\$ 5,720

There was an increase in revenues of \$403,992 and an increase in expenses of \$442,551 from fiscal year 2004. Of the increase in revenues, the foundation payments increased by \$278,576. Community Schools receive no support from tax revenues.

The expense for salaries increased by \$149,300 and the expense for fringe benefits increased by \$35,021 from fiscal year 2004. This was the first full fiscal year of operations. Material and supplies expense increased by \$77,311 due to additional material and supplies purchases. Depreciation expense increased by \$6,189.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEAR ENDED JUNE 30, 2005
UNAUDITED
(Continued)**

Capital Assets

At the end of fiscal year 2005 the School had \$27,251 (net of \$7,851 in accumulated depreciation) invested in furniture and equipment. Table 3 shows fiscal year 2005 balances compared to fiscal year 2004:

Table 3
Capital Asset at June 30, 2005
(Net of Depreciation)

	2005	2004
Furniture, Fixtures, and Equipment	<u>\$ 27,251</u>	<u>\$ 3,324</u>

For more information on capital assets see Note 5 to the basic financial statements.

Current Financial Issues

The School's financial relationship with the Lucas County Educational Service Center aids in the raising of the quality of financial records and strengthens internal controls. During the 2004-2005 school year, there were approximately 50 students enrolled in the School. The School receives its finances mostly from state aid. Per pupil aid for fiscal year 2005 amounted to \$5,058 per student.

See Note 16 for additional financial issues on the schools operations.

Contacting the School's Financial Management

This financial report is designed to provide our citizen's with a general overview of the Schools' finances and to show the Schools' accountability for the money it receives. If you have questions about this report or need additional information contact Dr. Cheryl Parchia of the ScholARTS Preparatory Middle School, 400 E. Town Street, Suite G-30, Columbus, Ohio 43215 or e-mail at dr.ctp@scolarts.org.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**STATEMENT OF NET ASSETS
AS OF JUNE 30, 2005**

Assets:

Current Assets:

Cash and Cash Equivalents	\$ 14,540
Intergovernmental Receivable	4,902
Prepaid Items	1,550
Total Current Assets	<u>20,992</u>

Noncurrent Assets:

Security Deposits	7,917
Capital Assets, Net of Accumulated Depreciation	27,251
Total Noncurrent Assets	<u>35,168</u>
Total Assets	<u>\$ 56,160</u>

Liabilities:

Current Liabilities:

Accounts Payable	\$ 36,961
Accrued Wages Payable	33,154
Intergovernmental Payable	13,164
Total Liabilities	<u>83,279</u>

Net Assets:

Invested in Capital Assets	27,251
Restricted for Other Purposes	885
Unrestricted	(55,255)
Total Net Assets	<u>\$ (27,119)</u>

See Accompanying Notes to the Basic Financial Statements

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005**

Operating Revenues:

Foundation Payments	\$ 278,576
Disadvantaged Pupil Impact Aid	9,790
Special Education	5,724
Food Services	180
Other Operating Revenues	1,639
Total Operating Revenues	<u>295,909</u>

Operating Expenses:

Salaries	149,300
Fringe Benefits	35,021
Purchased Services	203,575
Materials and Supplies	77,672
Depreciation	7,020
Other Operating Expenses	13,761
Total Operating Expenses	<u>486,349</u>
Operating Loss	<u>(190,440)</u>

Non-Operating Revenues and Expenses:

Operating Grants - Federal	154,523
Operating Grants - State	3,000
Contribution and Donations	561
Interest	22
Interest and Fiscal Charges	(505)
Total Non-Operating Revenues and (Expenses)	<u>157,601</u>
Change in Net Assets	(32,839)
Net Assets at Beginning of Year (See note 2H)	<u>5,720</u>
Net Assets at End of Year	<u>\$ (27,119)</u>

See Accompanying Notes to the Basic Financial Statements

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005**

Increase (Decrease) in Cash and Cash Equivalents

Cash Flows from Operating Activities:

Cash Received from State of Ohio	\$	291,308
Cash Received from Other Operating Revenue		1,819
Cash Payments to Suppliers for Goods and Services		(269,969)
Cash Payments to Employee for Services		(119,359)
Cash Payments for Employee Benefits		(18,644)
Net Cash Used for Operating Activities		(114,845)

Cash Flows from Noncapital Financing Activities:

Cash Received from Operating Grants - Federal		152,403
Cash Received from Operating Grants - State		3,000
Proceeds from Loans		4,400
Principal Payments		(4,400)
Interest Payments		(505)
Cash Received from Donations		561
Net Cash Provided by Noncapital Financing Activities		155,459

Cash Flows from Capital and Related Financing Activities:

Payments for Capital Acquisitions		(30,947)
Net Cash Used for Capital and Related Financing Activities		(30,947)

Cash Flows from Investing Activities:

Cash Received from Interest on Investments		22
Net Cash Provided by Investing Activities		22

Net Increase in Cash and Cash Equivalents		9,689
Cash and Cash Equivalents at Beginning of Year		4,851
Cash and Cash Equivalents at End of Year	\$	14,540

(Continued)

See Accompanying Notes to the Basic Financial Statements

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

Reconciliation of Operating Loss
to Net Cash Used for Operating Activities:

Operating Loss \$ (190,440)

Adjustments to Reconcile Operating Loss
to Net Cash Used for Operating Activities:

Depreciation	7,020
Changes in Assets and Liabilities:	
Increase in Intergovernmental Receivable	(2,782)
Increase in Prepaid Items	(1,550)
Increase in Security Deposits	(7,917)
Increase in Accounts Payable	34,506
Increase in Accrued Wages Payable	33,154
Increase in Intergovernmental Payable	13,164
	<hr/>

Total Adjustments

75,595

Net Cash Used for Operating Activities \$ (114,845)

See Accompanying Notes to the Basic Financial Statements

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
JUNE 30, 2005**

1. DESCRIPTION OF THE SCHOOL DISTRICT AND REPORTING ENTITY

The ScholARTS Preparatory Middle School (the School) is a nonprofit corporation established pursuant to Ohio Revised Code Sections 3314 and 1702, which is in the start up phase of operations. The School is an approved tax-exempt organization under Section 501(c)(3) of the Internal Revenue Code exclusively for educational purposes. Management is not aware of any course of action or series of events, which could adversely affect the School's tax-exempt status. The School's mission is for children to increase academic achievement, develop a community of scholars using the arts, and expose young children to a variety of options through an age-appropriate literacy based career center. The School, which is part of the State's education program, is independent of any school district and is nonsectarian in its programs, admission policies, employment practices, and all other operations. The School may acquire facilities as needed and contract for any services necessary for the operation of the school.

The School was approved for operation under a contract with the Lucas County Educational Service Center (the Sponsor) for a period of five years effective for the 2003-2004 academic school year. The Sponsor is responsible for evaluating the performance of the School and has the authority to deny renewal of the contract at its expiration or terminate the contract prior to its expiration. The sponsorship agreement states the Treasurer of the Sponsor should serve as the Chief Fiscal Officer (See Note 11).

The School operates under the direction of a five-member Board of Directors. The Board of Directors is responsible for carrying out the provisions of the contract, which include but are not limited to, state-mandated provisions regarding student population, curriculum, academic goals, performance standards, admission standards, and qualifications of teachers. The Governing Board controls the School's one instructional/support facility. Currently, the School currently is staffed by 3 non-certificated and 3 certificated full time teaching personnel and there was 48 students enrolled as of the end of the 2004-2005 school year.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the School have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to a governmental nonprofit organization. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The School also applies Financial Accounting Standards Board (FASB) statements and interpretations issued on or before November 30, 1989, to its proprietary activities, provided they do not conflict with or contradict GASB pronouncements. Following are the more significant of the School's accounting policies.

A. Basis of Presentation

The School's basic financial statements consist of a statement of net assets, a statement of revenues, expenses, and changes in net assets, and a statement of cash flows. The School's uses enterprise accounting to track and report on its financial activities. Enterprise fund reporting focuses on the determination of the change in net assets, financial position, and cash flows.

B. Measurement Focus

Enterprise accounting uses a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities are included on the statements of net assets. The statement of changes in net assets presents increases (i.e., revenues) and decreases (i.e., expenses) in net total assets. The statement of cash flow reflects how the School finances and meets its cash flow needs.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
JUNE 30, 2005
(Continued)**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Budgetary Process

Unlike other public schools located in the State of Ohio, community schools are not required to follow budgetary provisions set forth in Ohio Revised Code Chapter 5705, unless specifically provided in the School's contract with its Sponsor. The contract between the School and its Sponsor does prescribe an annual budget requirement in addition to preparing a five-year forecast, which is to be updated annually.

D. Cash and Investments

All monies received by the School are accounted for by the School's fiscal agent, the Lucas County Educational Service Center. All cash received by the fiscal agent is maintained in separate accounts in the School's name. Monies for the School are maintained in these accounts.

For presentation on the financial statements, investments of the cash management pool and investments with an original maturity of three months or less at the time they are purchased by the School are considered to be cash equivalents. Investments with an initial maturity of more than three months that are not purchased from the pool are reported as investments.

E. Capital Assets and Depreciation

All capital assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated capital assets are recorded at their fair market values as of the date received. The School maintains a capitalization threshold of \$150. The School does not possess any infrastructure.

Improvements are capitalized; the costs of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset's life are not.

All reported capital assets are depreciated. Improvements are depreciated over the remaining useful life of the related capital assets. Depreciation is computed using the straight-line method over the following useful lives:

<u>Description</u>	<u>Estimated Life</u>
Furniture, Fixtures, and Equipment	5

F. Intergovernmental Revenue

The School currently participates in the State Foundation Program, the State Disadvantaged Pupil Impact Aid (DPIA) Program, and the State Special Education Program. Revenues received from these programs are recognized as operating revenues (foundation payments) in the accounting period in which they are earned and become measurable.

Grants and entitlements are recognized as non-operating revenues in the accounting period in which all eligibility requirements have been met.

Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted, matching requirements, in which the School must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the School on a reimbursement basis.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
JUNE 30, 2005
(Continued)**

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

G. Prepaid Items

Prepayments represent cash disbursements, which have occurred and are therefore not current expendable resources. These items are reported as assets on the Statement of Net Assets, using the allocation method, which amortizes their cost over the periods benefiting from the advance payment.

H. Net Assets

Net assets represent the difference between assets and liabilities. Invested in Capital Assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction, or improvement of those assets. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the School or through external restrictions imposed by creditors, grantors or regulations of other governments.

For the fiscal year ended June 30, 2005, the School has presented for the first time basic financial statements in accordance with generally accepted accounting principles. In conjunction with this presentation, the School has changed its basis of accounting from a cash basis to accrual basis of accounting using an enterprise presentation for its basic financial statements. The restatement to beginning net assets is \$5,720.

I. Estimates

The preparation of the financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

J. Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the primary activities. For the School, these revenues are primarily the State Foundation program and the State Special Education program. Operating expenses are necessary costs incurred to provide the good or service that is the primary activity of the School. Revenues and expenses not meeting this definition are reported as non-operating.

K. Security Deposit

The School entered into a lease for the use of the building for the administration and instruction of the School. Based on the lease agreement, a security deposit was required to be paid at the signing of the agreement. This amount, totaling \$7,917, is held by the lessor. (See Note 10)

3. DEPOSITS

At June 30, 2005, the carrying amount of the School's deposits was \$14,540 and the bank balance was \$24,986. Based on the criteria described in GASB Statement No. 40, "Deposit and Investment Risk Disclosure," as of June 30, 2005, none of the bank balance was exposed to custodial risk as discussed below, while all of the bank balance was covered by the Federal Depository Insurance Corporation.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
JUNE 30, 2005
(Continued)**

3. DEPOSITS (Continued)

Custodial credit risk is the risk that in the event of bank failure, the School will not be able to recover deposits.

4. RECEIVABLES

Receivables at June 30, 2005, consisted of intergovernmental receivables arising from federal reimbursement. All receivables are considered collectable in full. A summary of the principal items of receivables follows:

Receivables	Amount
Foundation Reimbursement (See Note 13)	\$ 2,782
Federal Lunch Reimbursement - April	719
Federal Lunch Reimbursement - May	1,401
Total Receivables	\$ 4,902

5. CAPITAL ASSETS

Capital asset activity for the year ended June 30, 2005, was as follows:

	Balance 06/30/04	Additions	Deductions	Balance 06/30/05
Capital Assets Being Depreciation:				
Furniture, Fixtures, and Equipment	\$ 4,155	\$ 30,947	\$ -	\$ 35,102
Less Accumulated Depreciation:				
Furniture, Fixtures, and Equipment	(831)	(7,020)	-	(7,851)
Capital Assets, Net of A/D	\$ 3,324	\$ 23,927	\$ -	\$ 27,251

6. RISK MANAGEMENT

A. Insurance Coverage

The School is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During fiscal year 2005, the School contracted with the MFI Premium Budget and Philadelphia Insurance Company for general liability and director's and officer's insurance.

Coverage is as follows:

Commercial General Liability per occurrence	\$ 1,000,000
Commercial General Liability aggregate	1,000,000
Commercial General Liability Personal and Advertising Injury	1,000,000
Director's and Officer's Liability per occurrence	1,000,000
Director's and Officer's Liability aggregate	1,000,000

The School owns no property, but leases one facility located at 400 E. Town Street, Columbus, Ohio. (See Note 10)

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
JUNE 30, 2005
(Continued)**

6. RISK MANAGEMENT (Continued)

B. Worker's Compensation

The School pays the State Worker's Compensation System a premium for employee injury coverage. The premium is calculated by multiplying the monthly total gross payroll by a factor that is calculated by the State.

C. Employee Medical, Dental, and Life Benefits

The School contracted through a private insurance carrier to provide employee medical, dental, and vision insurance to its employees. The School pays the full amount of the monthly premiums for all selected coverage (medical, dental, and Life).

7. PENSION PLANS

A. School Employees Retirement System

The School contributes to the School Employees Retirement System (SERS), a cost-sharing multiple employer defined benefit pension plan. SERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by Chapter 3309 of the Ohio Revised Code. SERS issues a publicly available, stand-alone financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the School Employees Retirement System, 300 East Broad Street, Suite 100, Columbus, Ohio 43215-3476 or by calling (614) 222-5853.

Plan members are required to contribute 10 percent of their annual covered salary and the School District is required to contribute at an actuarially determined rate. The current School rate is 14 percent of annual covered payroll. A portion of the School's contribution is used to fund pension obligations with the remainder being used to fund health care benefits; for fiscal year 2005, 10.57 percent of annual covered salary was the portion used to fund pension obligations. The contribution requirements of plan members and employers are established and may be amended, up to statutory maximum amounts, by the SERS Retirement Board. The School's required contributions for pension obligations to SERS for the fiscal year ended June 30, 2005 was \$4,580; 36.98 percent has been contributed for fiscal year 2005.

B. State Teachers Retirement System

The School participates in the State Teachers Retirement System of Ohio (STRS Ohio), a cost-sharing, multiple-employer public employee retirement system. STRS Ohio provides retirement and disability benefits to members and death and survivor benefits to beneficiaries. STRS Ohio issues a stand-alone financial report that may be obtained by writing to STRS Ohio, 275 E. Broad St., Columbus, OH 43215-3371 or by calling (614) 227-4090.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
JUNE 30, 2005
(Continued)**

7. PENSION PLANS (Continued)

B. State Teachers Retirement System (Continued)

New members have a choice of three retirement plans, a Defined Benefit (DB) Plan, a Defined Contribution (DC) Plan and a Combined Plan. The DB plan offers an annual retirement allowance based on final average salary times a percentage that varies based on years of service, or an allowance based on member contributions and earned interest matched by STRS Ohio funds times an actuarially determined annuity factor. The DC Plan allows members to place all their member contributions and employer contributions equal to 10.5 percent of earned compensation into an investment account. Investment decisions are made by the member. A member is eligible to receive a retirement benefit at age 50 and termination of employment. The Combined Plan offers features of both the DC Plan and the DB Plan. In the Combined Plan, member contributions are invested by the member, and employer contributions are used to fund the defined benefit payment at a reduced level from the regular DB Plan. DC and Combined Plan members will transfer to the Defined Benefit Plan during their fifth year of membership unless they permanently select the DC or Combined Plan. Existing members with less than five years of service credit as of June 30, 2001, were given the option of making a one time irrevocable decision to transfer their account balances from the existing DB Plan into the DC Plan or the Combined Plan. This option expired on December 31, 2001. Benefits are established by Chapter 3307 of the Ohio Revised Code.

A DB or Combined Plan member with five or more years credited service who becomes disabled may qualify for a disability benefit. Eligible spouses and dependents of these active members who die before retirement may qualify for survivor benefits. Members in the DC Plan who become disabled are entitled only to their account balance. If a member dies before retirement benefits begin, the member's designated beneficiary is entitled to receive the member's account balance.

For the fiscal year ended June 30, 2005, plan members were required to contribute 10 percent of their annual covered salaries. The School was required to contribute 14 percent; 13 percent was the portion used to fund pension obligations. Contribution rates are established by the State Teachers Retirement Board, upon recommendation of its consulting actuary, not to exceed statutory maximum rates of 10 percent for members and 14 percent for employers. Chapter 3307 of the Ohio Revised Code provides statutory authority for member and employer contributions.

The School's required contributions for pension obligations to the DB Plan for the fiscal year ended June 30, 2005, was \$14,669; 92.10 percent has been contributed for fiscal year 2005.

8. POSTEMPLOYMENT BENEFITS

The School provides comprehensive health care benefits to retired teachers and their dependents through the State Teachers Retirement System (STRS), and to retired non-certified employees and their dependents through the School Employees Retirement System (SERS). Benefits include hospitalization, physicians' fees, prescription drugs and reimbursement of monthly Medicare premiums. Benefit provisions and the obligations to contribute are established by the Systems based on authority granted by State statute. Both systems are funded on a pay-as-you-go basis.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
JUNE 30, 2005
(Continued)**

8. POSTEMPLOYMENT BENEFITS (Continued)

STRS retirees who participated in the DB or combined plans and their dependents are eligible for health care coverage. The STRS Board has statutory authority over how much, if any, of the health care costs will be absorbed by STRS. All benefit recipients pay a portion of health care cost in the form of a monthly premium. By law, the cost of coverage paid from STRS funds is included in the employer contribution rate, currently 14 percent of covered payroll. For the fiscal year ended June 30, 2005, the STRS Board allocated employer contributions equal to 1 percent of covered payroll to the Health Care Reserve Fund. For the School, this amount equaled \$1,033 for fiscal year 2005.

STRS pays health care benefits from the Health Care Stabilization Fund. At June 30, 2004, (the latest information available) the balance in the Fund was \$3.1 billion. For the fiscal year ended June 30, 2004, net health care costs paid by STRS were \$268,739,000 and STRS had 111,853 eligible benefit recipients.

For SERS, coverage is made available to service retirees with ten or more fiscal years of qualifying service credit, and to disability and survivor benefit recipients. All retirees and beneficiaries are required to pay a portion of their premium for health care. The portion is based on years of service, Medicare eligibility, and retirement status. Premiums may be reduced for retirees whose household income falls below the poverty level.

After the allocation for basic benefits, the remainder of the employer's 14 percent contribution is allocated to providing health care benefits. For the fiscal year ended June 30, 2005, employer contributions to fund health care benefits were 3.43 percent of covered payroll, a decrease of 1.48 percent from fiscal year 2004. In addition, SERS levies a surcharge to fund health care benefits equal to 14 percent of the difference between a minimum pay and the member's pay, pro-rated for partial service credit. For fiscal year 2005, the minimum pay was established at \$27,400. However, the surcharge is capped at 2 percent of each employer's SERS salaries. For the 2005 fiscal year, School paid \$2,467 to fund health care benefits, including the surcharge.

The surcharge, added to the unallocated portion of the 14 percent employer contribution rate, provides for maintenance of the asset target level for the health care fund. The target level for the health care reserve is 150 percent of annual health care expenses. Expenses for health care for the fiscal year ended June 30, 2004 (the latest information available), were \$223,443,805 and the target level was \$335.2 million. At June 30, 2004, SERS had net assets available for payment of health care benefits of \$300.8 million. SERS has approximately 62,000 participants currently receiving health care benefits.

9. SHORT TERM DEBT

As stated in Note 15, during fiscal year ending June 30, 2005 the School entered into short term loan with CEO Dr. Cheryl Parchia for \$400. The School repaid this loan on February 15, 2005.

On December 8, 2004 the School borrowed \$4,000 on a MBNA Credit Card account through a cash advance. The repayment of this debt was made on March 15, 2005 and April 20, 2005.

10. OPERATING LEASE

In October 2004, the School entered into an operating lease for the period October 1, 2004 through September 30, 2005 with Capital South Community Redevelopment for the use of the School's facility. Payments made totaled \$79,287 for the fiscal year ended 2005.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
JUNE 30, 2005
(Continued)**

10. OPERATING LEASE (Continued)

In August of 2004, the School entered into a operating lease for a copier with the Xerox Corporation. Payments made totaled \$1,790 for the fiscal year.

11. FISCAL AGENT

The sponsorship agreement states the Treasurer of the Lucas County Educational Service Center shall serve as the Chief Fiscal Officer of the School. As part of this agreement, the School shall compensate the Lucas County Educational Service Center two percent (2%) of the per pupil allotment paid to the School from the State of Ohio. A total contract payment of \$8,397 was paid during the year, and a liability in the amount of \$1,254 was accrued as a liability for the fiscal year ended June 30, 2005.

The Treasurer shall perform all of the following functions while serving as the Chief Fiscal Officer of the School:

- Maintain custody of all funds received by the School in segregated accounts separate from the Sponsor or any other Community School's funds;
- Maintain all books and accounts of the School;
- Maintain all financial records of all state funds of the School and follow State Auditor procedures for receiving and expending state funds;
- Assist the School in meeting all financial reporting requirements established by the Auditor of Ohio;
- Invest funds of the School in the same manner as the funds of the Sponsor are invested, but the Treasurer shall not commingle the funds with any of the Sponsor or any other community school; and
- Pay obligations incurred by the School within a reasonable amount of time, not more than 14 calendar days after receipt of a properly executed voucher signed by the Chief Administrative Officer of the School so long as the proposed expenditure is within the approved budget and funds are available.

12. PURCHASED SERVICES

For the period July 1, 2004 through June 30, 2005, purchased service expenses were payments for services rendered by various vendors, and were as follows:

PURCHASED SERVICES	
Professional and Technical Services	\$ 73,857
Property Services	79,663
Travel Mileage/Meeting Expense	428
Communications	18,375
Contracted Craft or Trade Services	12,345
Transportation Services	14,500
Other Purchased Services	4,407
Total Purchased Services	<u>\$ 203,575</u>

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
JUNE 30, 2005
(Continued)**

13. CONTINGENCIES

A. Grants

The School received financial assistance from Federal and State agencies in the form of grants. The disbursement of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and is subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the School. However, in the opinion of management, any such disallowed claims will not have an adverse material effect on the overall financial position of the School at June 30, 2005.

B. School Funding

The Ohio Department of Education reviews enrollment data and full-time equivalency (FTE) calculations made by the schools. These reviews are conducted to ensure the schools are reporting accurate student enrollment data to the State, upon which state foundation funding is calculated.

ODE has conducted a review of the School's 2005 student enrollment data and FTE calculations. The final review for fiscal year 2005 reflected that the Ohio Department of Education owed the School \$2,782 as of June 30, 2005. This amount is reflected as part of intergovernmental receivable on the statement of net assets.

C. Pending Litigation

A suit was filed in Franklin County common Pleas Court on May 14, 2001 alleging Ohio's Community (i.e., Charter) Schools program violates the state Constitution and state laws. On April 21, 2003 the court dismissed the counts containing constitutional claims and stayed the other counts pending appeal of the constitutional issues. The plaintiffs appealed to the Court of Appeals, the issues have been briefed, and the case was heard on November 18th, 2003. On August 24, 2004, the Court of Appeals rendered a decision that Community Schools are a part of the state public educational system and this matter was sent to the Ohio Supreme Court. The Ohio Supreme Court accepted the appeal from the Court of Appeals for review on February 16, 2005. Oral argument occurred November 29, 2005. The effect of this suit, if any on ScholARTS Preparatory Middle School is not presently determinable.

14. RELATED PARTY TRANSACTIONS

Dr. Cheryl Parchia, Founder and CEO of the School, also is president of the board of directors. During fiscal year 2005, Dr. Parchia received a \$30,000 salary, and \$23,401 for curriculum development and school startup consulting and reimbursement of miscellaneous expenses. Dr. Parchia received no compensation for being board president.

In addition on January 30, 2005, Dr. Cheryl Parchia provided a \$400 loan to the School to cover operational costs. The loan to the School was to cover operational costs. The loan was paid off on February 15, 2005.

The board secretary of the School & Board of Director is the daughter of Dr. Cheryl Parchia. During fiscal year 2005, a \$1,500 stipend was paid to her as compensation for her position.

**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
JUNE 30, 2005
(Continued)**

15. SUBSEQUENT EVENT

On September 6, 2005, the Ohio Department of Education authorized the merger of the ScholARTS Career Center for Children and ScholARTS Preparatory Middle School prior to the start of the 2005-2006 academic year. The merger resulted in a new entity known as the ScholARTS Preparatory and Career Center for Children. The Lucas County Educational Service Center closed financial records of the ScholARTS Career Center for Children on September 16, 2005 and as of this date the ScholARTS Preparatory and Career Center for Children assumed the assets and liabilities of the ScholARTS Career Center for Children. The most significant liability assumed by the ScholARTS Preparatory and Career Center for Children is \$77,231 owed to the Ohio Department of Education for over payment of state foundation from the period of July 1, 2005 through September 16, 2005. The School has asked the Ohio Department of Education to repay this loan over a 24 month period to alleviate cash flow problems and is attempting to negotiate the repayment.

On August 15, 2005, Board of Director and CEO, Dr. Cheryl Parchia loaned the School \$2,000. As of February 27, 2006, \$1,500 of this loan has been repaid.

In October 2005, Board of Director, Dr. Billie Thomas loaned the School \$1,000 that was repaid by the School on February 7, 2006.

On December 7, 2005 the Board of Directors voted to decrease all administrative and teaching staff salaries by 10% until an increase in funding could be maintained. This action was amended on January 25, 2006 when teaching contracts were set at \$32,000.

16. MANAGEMENT PLAN

The School financial records and Board of Director's actions taken subsequent to June 30, 2005, as described in Note 15, indicate that the School is having difficulties meeting operational expenses. On December 7, 2005 the Board of Directors voted to decrease all administrative and teaching staff salaries by 10% until an increase in funding could be found. On September 16, 2005, the Board also assumed the liabilities of ScholARTS Career Center.

The Board of Directors have drafted a fiscal plan and five year forecast. The fiscal plan includes applying for and obtaining governmental grants and private and corporate donations to aid in operational costs. In addition, the School will be spending additional funds to pay for advertising to recruit students and increase the amount of foundation receipts collected. The Board has requested the outstanding liability of \$77,231 owed to the Ohio Department of Education be repaid over 24 months and the Ohio Department of Education has agreed to this plan (See Note 15).



**Auditor of State
Betty Montgomery**

**INDEPENDENT ACCOUNTANTS' REPORT ON INTERNAL CONTROL OVER
FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS
REQUIRED BY *GOVERNMENT AUDITING STANDARDS***

ScholARTS Preparatory Middle School
Franklin County
400 E. Town Street
Columbus, Ohio 43215

To the Board of Directors:

We have audited the accompanying basic financial statements of the ScholARTS Preparatory Middle School, Franklin County, Ohio (the School) as of and for the year ended June 30, 2005 and have issued our report thereon dated February 27, 2006 wherein we noted the School is experiencing financial difficulties. 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 the Comptroller General of the United States' *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the School's internal control over financial reporting to determine our auditing procedures in order to express our opinion on the financial statements and not to opine on the internal control over financial reporting. Our consideration of the internal control would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts material to the financial statements we audited may occur and not be timely detected by employees when performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider material weaknesses. In a separate letter to the School's management dated February 27, 2006, we reported other matters involving internal control over financial reporting we did not deem reportable conditions.

Compliance and Other Matters

As part of reasonably assuring whether the School's financial statements are free of material misstatement, we tested its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could directly and materially affect 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 an opinion. The results of our tests disclosed no instances of noncompliance or other matters we must report under *Government Auditing Standards*.

35 N. Fourth St. / Second Floor / Columbus, OH 43215
Telephone: (614) 466-3402 (800) 443-9275 Fax: (614) 728-7199
www.auditor.state.oh.us

We intend this report solely for the information and use of management and the Board of Directors. It is not intended for anyone other than these specified parties.

A handwritten signature in black ink that reads "Betty Montgomery". The signature is written in a cursive, flowing style.

Betty Montgomery
Auditor of State

February 27, 2006



**Auditor of State
Betty Montgomery**

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800-282-0370

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**SCHOLARTS PREPARATORY MIDDLE SCHOOL
FRANKLIN COUNTY**

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

**CERTIFIED
JUNE 27, 2006**