

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

SINGLE AUDIT

FOR THE YEAR ENDED JUNE 30, 2005



**Auditor of State
Betty Montgomery**

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

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**Auditor of State
Betty Montgomery**

INDEPENDENT ACCOUNTANTS' REPORT

Erie-Huron-Ottawa Educational Service Center
Erie County
2900 Columbus Avenue
Sandusky, Ohio 44870-5569

To the Governing Board:

We have audited the accompanying financial statements of the governmental activities, the major fund, and the aggregate remaining fund information of the Erie-Huron-Ottawa Educational Service Center, Erie County, Ohio (the Service Center), as of and for the year ended June 30, 2005, which collectively comprise the Service Center's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Service Center's management. Our responsibility is to express opinions 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 opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the major fund, and the aggregate remaining fund information of the Erie-Huron-Ottawa Educational Service Center, Erie County, Ohio, as of June 30, 2005, and the respective changes in financial position, thereof and the budgetary comparison for the General Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 3, the Service Center adopted Governmental Accounting Standards Board Statement 40 and GASB Technical Bulletin 2004-2.

In accordance with *Government Auditing Standards*, we have also issued our report dated May 8, 2006, on our consideration of the Service Center'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 and Analysis is not a required part of the basic financial statements but is supplementary information accounting principles generally accepted in the United States of America 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.

We conducted our audit to opine on the financial statements that collectively comprise the Service Center's basic financial statements. The federal awards expenditure schedule is required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. We subjected the federal awards expenditure schedule to the auditing procedures applied in the audit of the basic financial statements. In our opinion, this information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.



Betty Montgomery
Auditor of State

May 8, 2006

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

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

The discussion and analysis of the Erie-Huron-Ottawa Educational Service Center's ("the ESC") financial performance provides an overall review of the ESC's financial activities for the fiscal year ended June 30, 2005. The intent of this discussion and analysis is to look at the ESC's financial performance as a whole; readers should also review the basic financial statements and the notes to the basic financial statements to enhance their understanding of the ESC's financial performance.

Financial Highlights

Key financial highlights for 2005 are as follows:

- In total, net assets of governmental activities increased \$535,651 which represents a 111.58% increase from 2004.
- General revenues accounted for \$2,890,601 in revenue or 16.17% of all revenues. Program specific revenues in the form of charges for services and sales, grants and contributions accounted for \$14,990,318 or 83.83% of total revenues of \$17,880,919.
- The ESC had \$17,345,268 in expenses related to governmental activities; only \$14,990,318 of these expenses was offset by program specific charges for services, grants or contributions. General revenues supporting governmental activities (unrestricted grants and entitlements) of \$2,890,601 were not adequate to provide for these programs.
- The ESC's only major governmental fund is the general fund. The general fund had \$15,886,682 in revenues and other financing sources and \$15,115,122 in expenditures and other financing uses. During fiscal 2005, the general fund's fund balance increased \$771,560 from \$364,171 to \$1,135,731.

Using these Basic Financial Statements (BFS)

This annual report consists of a series of financial statements and notes to those statements. These statements are organized so the reader can understand the ESC as a financial whole, an entire operating entity. The statements then proceed to provide an increasingly detailed look at specific financial activities.

The *Statement of Net Assets* and *Statement of Activities* provide information about the activities of the whole ESC, presenting both an aggregate view of the ESC's finances and a longer-term view of those finances. Fund financial statements provide the next level of detail. For governmental funds, these statements tell how services were financed in the short-term as well as what remains for future spending. The fund financial statements also look at the ESC's most significant funds with all other nonmajor funds presented in total in one column. In the case of the ESC, the general fund is by far the most significant fund, and the only governmental fund reported as a major fund.

Reporting the ESC as a Whole

Statement of Net Assets and the Statement of Activities

While this document contains the large number of funds used by the ESC to provide programs and activities, the view of the ESC as a whole looks at all financial transactions and asks the question, "How did we do financially during 2005?" The *Statement of Net Assets* and the *Statement of Activities* answer this question. These statements include *all assets, liabilities, revenues and expenses* using the *accrual basis of accounting* similar to the accounting used by most private-sector companies. This basis of accounting will take into account all of the current year's revenues and expenses regardless of when cash is received or paid.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

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

These two statements report the ESC's *net assets* and changes in those assets. This change in net assets is important because it tells the reader that, for the ESC as a whole, the *financial position* of the ESC has improved or diminished. The causes of this change may be the result of many factors, some financial, some not. Non-financial factors include increased or decreased services desired by school districts, state budget cuts, required educational programs and other factors.

In the Statement of Net Assets and the Statement of Activities, the Governmental Activities include the ESC's programs and services, including instruction, support services, and other operations.

Reporting the ESC's Most Significant Funds

Fund Financial Statements

The analysis of the ESC's major governmental fund begins on page 9. Fund financial reports provide detailed information about the ESC's major funds. The ESC uses many funds to account for a multitude of financial transactions. However, these fund financial statements focus on the ESC's most significant funds. The ESC's only major governmental fund is the general fund.

Governmental Funds

Most of the ESC's activities are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end available for spending in future periods. These funds are reported using an accounting method called *modified accrual* accounting, which measures cash and all other *financial assets* that can readily be converted to cash. The governmental fund financial statements provide a detailed *short-term* view of the ESC's general government operations and the basic services it provides. Governmental fund information helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance educational 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 basic financial statements.

Reporting the ESC's Fiduciary Responsibilities

The ESC is the fiscal agent of the area A-site, NOECA. This activity is presented as an investment trust fund. The ESC also maintains agency funds to account for monies due to other governments, individuals or private organizations. All of the ESC's fiduciary activities are reported in a separate Statement of Fiduciary Net Assets. The investment trust funds activities for fiscal 2005 are also reported in a separate Statement of Changes in Fiduciary Net Assets. These activities are excluded from the ESC's other financial statements because the assets cannot be utilized by the ESC to finance its operations.

Notes to the Basic Financial Statements

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

The ESC as a Whole

The Statement of Net Assets provides the perspective of the ESC as a whole.

The table below provides a summary of the ESC's net assets for 2005 and 2004.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

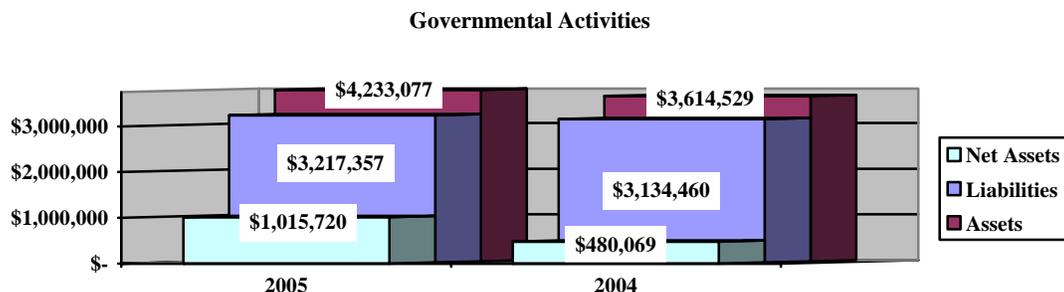
**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
UNAUDITED
(Continued)**

	Net Assets	
	Governmental Activities 2005	Governmental Activities 2004
<u>Assets</u>		
Current and other assets	\$ 3,863,807	\$ 3,182,812
Capital assets, net	<u>369,270</u>	<u>431,717</u>
Total assets	<u>4,233,077</u>	<u>3,614,529</u>
<u>Liabilities</u>		
Current liabilities	1,989,898	2,091,925
Long-term liabilities	<u>1,227,459</u>	<u>1,042,535</u>
Total liabilities	<u>3,217,357</u>	<u>3,134,460</u>
<u>Net Assets</u>		
Invested in capital assets	369,270	431,717
Restricted	241,590	2,645
Unrestricted	<u>404,860</u>	<u>45,707</u>
Total net assets	<u>\$ 1,015,720</u>	<u>\$ 480,069</u>

Over time, net assets can serve as a useful indicator of a government's financial position. At June 30, 2005, the ESC's assets exceeded liabilities by \$1,015,720. Of this total, \$241,590 is restricted in use.

At year-end, capital assets represented 8.72% of total assets. Capital assets include a building, furniture and equipment and vehicles. Capital assets, net of accumulated depreciation at June 30, 2005, were \$369,270. These capital assets are used to provide the ESC's services and are not available for future spending.

A portion of the ESC's net assets, \$241,590, represents resources that are subject to external restriction on how they may be used. The remaining balance of unrestricted net assets is \$404,860 may be used to meet the ESC's ongoing obligations to the students and creditors.



**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
UNAUDITED
(Continued)**

The table below shows the change in net assets for fiscal year 2005 and 2004.

	Change in Net Assets	
	Governmental Activities 2005	Governmental Activities 2004
<u>Revenues</u>	<u>2005</u>	<u>2004</u>
Program revenues:		
Charges for services and sales	\$ 13,074,688	\$ 12,067,633
Operating grants and contributions	1,915,630	1,923,784
Capital grants and contributions		15,827
General revenues:		
Grants and entitlements	2,820,433	3,322,948
Investment earnings	69,532	31,236
Gain on sale of capital assets		230
Other	<u>636</u>	<u>765</u>
Total revenues	<u>17,880,919</u>	<u>17,362,423</u>

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
UNAUDITED
(Continued)**

	Change in Net Assets	
	Governmental Activities <u>2005</u>	Governmental Activities <u>2004</u>
<u>Expenses</u>		
Program expenses:		
Instruction:		
Regular	\$ 70,655	\$ 111,266
Special	5,064,174	4,906,527
Support services:		
Pupil	3,932,649	4,140,717
Instructional staff	6,326,864	6,924,671
Board of education	88,968	66,659
Administration	715,507	718,432
Fiscal	362,987	338,227
Business	202,743	175,783
Operations and maintenance	395,811	295,940
Pupil transportation	271	2,102
Central	90,463	55,923
Operations of non-instructional services	47,132	20,344
Extracurricular activities	6,618	8,816
Intergovernmental	<u>40,426</u>	<u>93,312</u>
Total expenses	<u>17,345,268</u>	<u>17,858,719</u>
Change in net assets	535,651	(496,296)
Net assets at beginning of year	<u>480,069</u>	<u>976,365</u>
Net assets at end of year	<u>\$ 1,015,720</u>	<u>\$ 480,069</u>

Governmental Activities

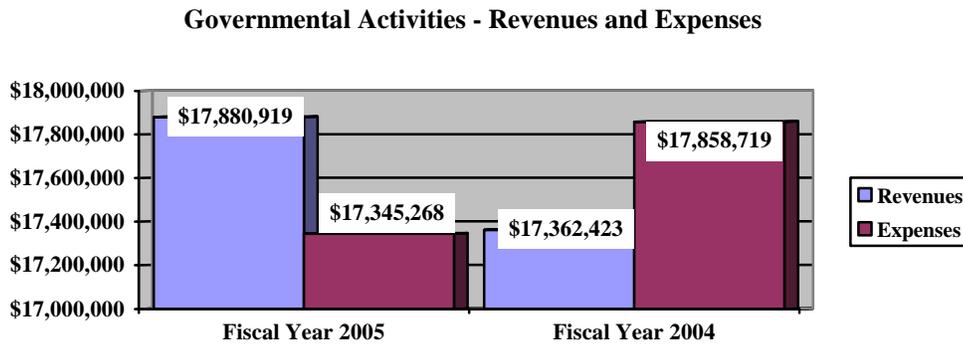
Net assets of the ESC's governmental activities increased \$535,651. Total governmental expenses of \$17,345,268 were offset by program revenues of \$14,990,318 and general revenues of \$2,890,601. Program revenues supported 86.42% of the total governmental expenses. The reason for the increase in net assets can be attributed to a large increase in services provided and a reduction in workforce.

The primary sources of revenue for governmental activities are derived from contracted fees for services provided to other entities. This revenue source represents 73.12% of total governmental revenue.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

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

The graph below presents the ESC's governmental activities revenue and expenses for fiscal years 2005 and 2004.



The Statement of Activities shows the cost of program services and the charges for services and grants offsetting those services. The following table shows, for governmental activities, the total cost of services and the net cost of services. That is, it identifies the cost of these services supported by unrestricted State grants and entitlements, and other general revenues not restricted to a specific program.

Governmental Activities

	<u>Total Cost of Services 2005</u>	<u>Net Cost of Services 2005</u>	<u>Total Cost of Services 2004</u>	<u>Net Cost of Services 2004</u>
Program expenses				
Instruction:				
Regular	\$ 70,655	\$ 9,672	\$ 111,266	\$ 12,673
Special	5,064,174	404,344	4,906,527	787,756
Support services:				
Pupil	3,932,649	643,954	4,140,717	847,152
Instructional staff	6,326,864	951,278	6,924,671	1,278,401
Board of education	88,968	14,605	66,659	66,659
Administration	715,507	66,718	718,432	93,056
Fiscal	362,987	23,331	338,227	287,919
Business	202,743	49,672	175,783	175,783
Operations and maintenance	395,811	177,876	295,940	274,605
Pupil transportation	271	271	2,102	2,102
Central	90,463	12,827	55,923	55,923
Operation of non-instructional services	47,132	(14,596)	20,344	(48,739)
Extracurricular activities	6,618	4,700	8,816	(2,888)
Intergovernmental	40,426	10,298	93,312	21,073
Total expenses	<u>\$ 17,345,268</u>	<u>\$ 2,354,950</u>	<u>\$ 17,858,719</u>	<u>\$ 3,851,475</u>

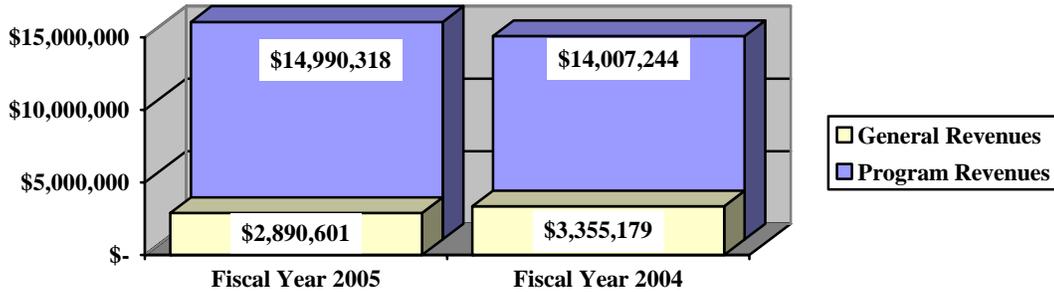
**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

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

For all governmental activities, program revenue support is 86.42%. The primary support of the ESC is contracted fees for services provided to other districts.

The graph below presents the ESC's governmental activities revenue for fiscal year 2005 and 2004.

Governmental Activities - General and Program Revenues



The ESC's Funds

The ESC's governmental funds reported a combined fund balance of \$1,471,040, which is higher than last year's total of \$642,749 (as restated, see Note 3.A of the notes to the financial statements). The schedule below indicates the fund balance and the total change in fund balance as of June 30, 2005 and 2004.

	Fund Balance June 30, 2005	Restated Fund Balance June 30, 2004	Increase
General	\$ 1,135,731	\$ 364,171	\$ 771,560
Other Governmental	335,309	278,578	56,731
Total	\$ 1,471,040	\$ 642,749	\$ 828,291

General Fund

The ESC's general fund balance increased by \$771,560. The increase in fund balance can be attributed to a decrease in costs associated with contract services provided to Districts. The table that follows assists in illustrating the financial activities and fund balance of the general fund.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

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

	2005 <u>Amount</u>	Restated 2004 <u>Amount</u>	Percentage <u>Change</u>
<u>Revenues</u>			
Tuition	\$ 32,262	\$ 21,134	52.65 %
Services provided to other entities	12,669,279	11,696,834	8.31 %
Earnings on investments	69,024	31,020	122.51 %
Intergovernmental	3,087,861	2,965,287	4.13 %
Other revenues	<u>27,922</u>	<u>34,954</u>	(20.12) %
Total	<u>\$ 15,886,348</u>	<u>\$ 14,749,229</u>	7.71 %
<u>Expenditures</u>			
Instruction	\$ 4,066,913	\$ 4,105,042	(0.93) %
Support services	10,898,849	11,186,796	(2.57) %
Facilities acquisition and construction	<u>138,772</u>	<u>140,224</u>	(1.04) %
Total	<u>\$ 15,104,534</u>	<u>\$ 15,432,062</u>	(2.12) %

The increase in earnings on investments can be attributed to the increasing interest rates for the ESC's investments.

General Fund Budgeting Highlights

The ESC's budget is prepared according to guidelines established by the Governing Board and is based on accounting for certain transactions on a basis of cash receipts, disbursements and encumbrances. The most significant budgeted fund is the general fund.

During the course of fiscal 2005, the ESC did not amend its general fund budgeted revenues. For the general fund, original and final budgeted revenues and other financing sources were \$15,687,117. Actual revenues and other financing sources for fiscal 2005 were \$15,828,845. This represents a \$141,728 increase over the original and final budgeted revenues. The ESC's actual revenue from state sources was \$438,560 less than anticipated. This was due to a procedural change in posting some school foundation revenue from a state source to a local source. The ESC's actual revenue from federal sources was \$510,518 more than anticipated due to increased amounts received from the Title XIX (Medicaid) Federal Program.

General fund original and final budgeted expenditures and other financing uses were \$17,601,435. The actual budget basis expenditures and other financing uses for fiscal year 2005 totaled \$15,360,591, which was \$2,240,844 less than the final budget appropriations. The ESC budgeted \$882,073 for contingency purposes as miscellaneous use of funds and never had to use this account. Also \$1,218,501 was not spent from the budgets of Special Instruction and Support Services for Pupil and Instructional Staff due to a reduction in staff and some services not needed as anticipated.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

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

Capital Assets

At the end of fiscal 2005, the ESC had \$369,270 invested in buildings, furniture and equipment, and vehicles. This entire amount is reported in governmental activities. The following table shows fiscal 2005 balances compared to 2004:

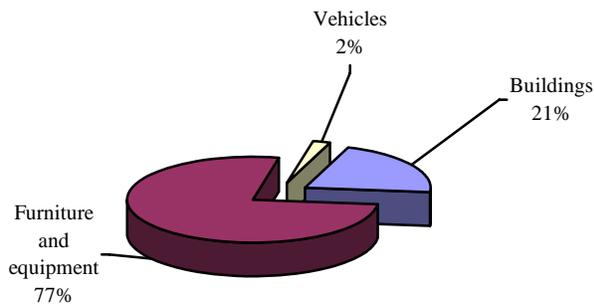
**Capital Assets at June 30
(Net of Depreciation)**

	<u>Governmental Activities</u>	
	<u>2005</u>	<u>2004</u>
Buildings	\$ 78,900	\$ 80,700
Furniture and equipment	281,694	336,826
Vehicles	<u>8,676</u>	<u>14,191</u>
Total	<u>\$ 369,270</u>	<u>\$ 431,717</u>

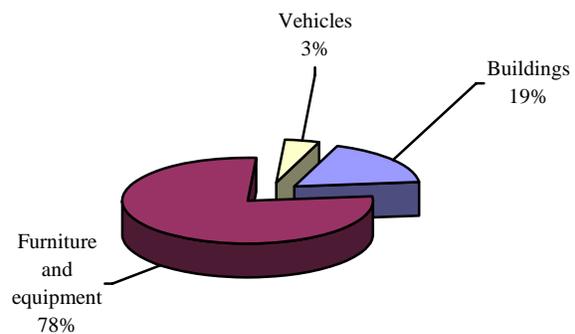
Total additions to capital assets for 2005 were \$39,062. A total of \$100,793 in depreciation expense was recognized for fiscal 2005.

The graphs below present the District's capital assets for fiscal 2005 and fiscal 2004.

**Capital Assets - Governmental Activities
2005**



**Capital Assets - Governmental Activities
2004**



See Note 8 to the basic financial statements for additional information on the ESC's capital assets.

Debt

The ESC had no long-term debt outstanding at year-end.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

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

Current Financial Related Activities

The Erie-Huron-Ottawa Educational Service Center relies heavily on contracts with local, city and exempted village school districts in the three-county area, state foundation revenue, and grants. Contracts with participating districts are expected to increase in fiscal year 2005 and beyond due to additional service requests from districts. The ESC also looks to expand providing fiscal, administrative and other services to entities. Currently some of those entities are the Northern Ohio Educational Computer Association, Bay Area Gas Consortium, and Ohio Effective Schools. These new contracts and expanded services along with the ESC's cash balance will provide the necessary funds to meet operating expenses in the future.

One challenge that is being faced by Educational Service Centers is the legislation regarding Ohio's Regional Education Delivery System and the implementation of that system by the Ohio Department of Education. This system will directly affect the Educational Service Centers and their funding mechanism. The Ohio Department of Education has submitted a report to the legislature. What effect this legislation will have on future state funding and on ESC financial operations is uncertain at this time.

Under state law, the County Commissioners are no longer required to provide rent-free space to ESC's. The Erie-Huron-Ottawa ESC Governing Board has negotiated a four-year rental agreement, however beyond that there may be a need to acquire new space or to pay a much higher rent for our current space.

Another challenge facing the Erie-Huron-Ottawa Educational Service Center is the declining enrollment in Erie, Huron, and Ottawa Counties over the past several years and the projected decline in the future. State foundation funding is based on the ADM of the school districts in the counties, so the continued decline will directly impact state funding.

Contacting the ESC's Financial Management

This financial report is designed to provide the citizen's supported by the districts, and investors and creditors with a general overview of the ESC's finances and to show the ESC's accountability for the money it receives. If you have questions about this report or need additional financial information contact Ms. Betty Schwiefert, Treasurer, Erie-Huron-Ottawa ESC, 2900 S. Columbus Avenue, Sandusky, Ohio 44870-5569 or by calling (419) 625-6274.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

STATEMENT OF NET ASSETS
JUNE 30, 2005

	Governmental Activities
Assets:	
Equity in pooled cash and cash equivalents.	\$ 2,895,560
Receivables:	
Accounts	6,566
Intergovernmental	936,721
Prepayments.	24,960
Depreciable capital assets, net	369,270
 Total assets	 4,233,077
Liabilities:	
Accounts payable	29,047
Accrued wages and benefits	1,600,197
Pension obligation payable.	280,343
Intergovernmental payable	80,311
Long-term liabilities:	
Due within one year.	226,704
Due within more than one year	1,000,755
 Total liabilities	 3,217,357
Net Assets:	
Invested in capital assets	369,270
Restricted for:	
Permanent endowment	2,645
Locally funded programs.	98,200
State funded programs.	35,313
Federally funded programs.	104,316
Other purposes.	1,116
Unrestricted.	404,860
 Total net assets	 \$ 1,015,720

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

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

		Program Revenues		Net (Expense) Revenue and Changes in Net Assets
	Expenses	Charges for Services and Sales	Operating Grants and Contributions	Governmental Activities
Governmental activities:				
Instruction:				
Regular	\$ 70,655	\$ 34,604	\$ 26,379	\$ (9,672)
Special	5,064,174	3,680,992	978,838	(404,344)
Support services:				
Pupil.	3,932,649	3,217,013	71,682	(643,954)
Instructional staff	6,326,864	4,938,232	437,354	(951,278)
Board of education	88,968	74,363		(14,605)
Administration.	715,507	393,092	255,697	(66,718)
Fiscal.	362,987	282,520	57,136	(23,331)
Business.	202,743	153,071		(49,672)
Operations and maintenance	395,811	217,935		(177,876)
Pupil transportation.	271			(271)
Central	90,463	77,636		(12,827)
Operation of non-instructional services.	47,132		61,728	14,596
Extracurricular activities.	6,618	1,918		(4,700)
Intergovernmental	40,426	3,312	26,816	(10,298)
Total governmental activities	\$ 17,345,268	\$ 13,074,688	\$ 1,915,630	(2,354,950)
General Revenues:				
Grants and entitlements not restricted to specific programs				2,820,433
Investment earnings				69,532
Miscellaneous				636
Total general revenues				2,890,601
Change in net assets				535,651
Net assets at beginning of year.				480,069
Net assets at end of year				\$ 1,015,720

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2005

	General	Other Governmental Funds	Total Governmental Funds
Assets:			
Equity in pooled cash and cash equivalents	\$ 2,532,228	\$ 363,332	\$ 2,895,560
Receivables:			
Accounts	6,566		6,566
Intergovernmental	810,877	125,844	936,721
Prepayments	24,943	17	24,960
	<u>\$ 3,374,614</u>	<u>\$ 489,193</u>	<u>\$ 3,863,807</u>
Liabilities:			
Accounts payable.	\$ 3,857	\$ 25,190	\$ 29,047
Accrued wages and benefits	1,526,195	74,001	1,600,196
Compensated absences payable	79,795		79,795
Pension obligation payable	270,526	9,817	280,343
Intergovernmental payable.	76,454	3,858	80,312
Deferred revenue.	282,056	41,018	323,074
	<u>2,238,883</u>	<u>153,884</u>	<u>2,392,767</u>
Fund Balances:			
Reserved for encumbrances	133,651	81,013	214,664
Reserved for prepayments	24,943	17	24,960
Reserved for principal endowment.		2,645	2,645
Unreserved, undesignated, reported in:			
General fund	977,137		977,137
Special revenue funds.		251,634	251,634
	<u>1,135,731</u>	<u>335,309</u>	<u>1,471,040</u>
Total fund balances	<u>\$ 1,135,731</u>	<u>\$ 335,309</u>	<u>\$ 1,471,040</u>
Total liabilities and fund balances.	<u>\$ 3,374,614</u>	<u>\$ 489,193</u>	<u>\$ 3,863,807</u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

RECONCILIATION OF TOTAL GOVERNMENTAL FUND BALANCES TO
NET ASSETS OF GOVERNMENTAL ACTIVITIES
JUNE 30, 2005

Total governmental fund balances	\$	1,471,040
<i>Amounts reported for governmental activities in the statement of net assets are different because:</i>		
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds.		369,270
Other long-term assets are not available to pay for current- period expenditures and therefore are deferred in the funds.		
Accounts	\$	38,470
Intergovernmental		<u>284,604</u>
Total		323,074
Long-term liabilities are not due and payable in the current period and therefore are not reported in the funds.		<u>(1,147,664)</u>
Net assets of governmental activities	\$	<u><u>1,015,720</u></u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

	<u>General</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Revenues:			
From local sources:			
Services provided to other entities	\$ 12,669,279	\$ 175,053	\$ 12,844,332
Tuition	32,262		32,262
Earnings on investments	69,024	508	69,532
Extracurricular		16,658	16,658
Contributions and donations		16,825	16,825
Other local revenues	27,922	1,026	28,948
Intergovernmental - intermediate sources		144,008	144,008
Intergovernmental - state.	2,254,557	1,327,102	3,581,659
Intergovernmental - federal	833,304	386,287	1,219,591
Total revenue.	<u>15,886,348</u>	<u>2,067,467</u>	<u>17,953,815</u>
Expenditures:			
Current:			
Instruction:			
Regular.		66,816	66,816
Special	4,066,913	925,938	4,992,851
Support Services:			
Pupil	3,816,788	89,631	3,906,419
Instructional staff	5,771,579	467,160	6,238,739
Board of education	88,968		88,968
Administration	434,222	237,251	671,473
Fiscal	336,850	57,341	394,191
Business.	183,134		183,134
Operations and maintenance	260,738		260,738
Central	6,570	83,011	89,581
Operation of non-instructional services.		47,132	47,132
Extracurricular activities		6,618	6,618
Facilities acquisition and construction	138,772		138,772
Intergovernmental pass through.		40,426	40,426
Total expenditures.	<u>15,104,534</u>	<u>2,021,324</u>	<u>17,125,858</u>
Excess of revenues over expenditures.	<u>781,814</u>	<u>46,143</u>	<u>827,957</u>
Other financing sources (uses):			
Transfers in.		10,588	10,588
Transfers out	(10,588)		(10,588)
Sale of capital assets	334		334
Total other financing sources (uses).	<u>(10,254)</u>	<u>10,588</u>	<u>334</u>
Net change in fund balances.	771,560	56,731	828,291
Fund balances at beginning of year (restated). .	<u>364,171</u>	<u>278,578</u>	<u>642,749</u>
Fund balances at end of year	<u>\$ 1,135,731</u>	<u>\$ 335,309</u>	<u>\$ 1,471,040</u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

Net change in fund balances - total governmental funds \$ 828,291

Amounts reported for governmental activities in the statement of activities are different because:

Government funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets are allocated over their estimated useful lives as depreciation expense. This is the amount by which depreciation exceeded capital outlays in the current period.

Capital asset additions	\$	39,062	
Current year depreciation		<u>(100,793)</u>	
 Total			 (61,731)

Governmental funds only report the disposal of capital assets to the extent proceeds are received from the sale. In the statement of activities, a gain or loss is reported for each disposal. (716)

Revenues in the statement of activities that do not provide current financial resources are not reported as revenues in the funds.

Intergovernmental		(128,445)	
Accounts receivable		<u>48,610</u>	
 Total			 (79,835)

Some expenses reported in the statement of activities do not require the use of financial resources and therefore are not reported as expenditures in governmental funds. (150,358)

Change in net assets of governmental activities \$ 535,651

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN
FUND BALANCE - BUDGET AND ACTUAL (NON-GAAP BUDGETARY BASIS)
GENERAL FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2005**

	<u>Budgeted Amounts</u>			Variance with Final Budget Positive (Negative)
	<u>Original</u>	<u>Final</u>	<u>Actual</u>	
Revenues:				
From local sources:				
Services provided to other entities.	\$ 12,403,275	\$ 12,403,275	\$ 12,406,070	\$ 2,795
Tuition.	20,000	20,000	32,340	12,340
Earnings on investments.	30,500	30,500	69,024	38,524
Other local revenues.	27,725	27,725	27,725	
Intergovernmental - intermediate sources.	2,500	2,500		(2,500)
Intergovernmental - state	2,693,117	2,693,117	2,254,557	(438,560)
Intergovernmental - federal.	500,000	500,000	1,010,518	510,518
Total revenue	<u>15,677,117</u>	<u>15,677,117</u>	<u>15,800,234</u>	<u>123,117</u>
Expenditures:				
Current:				
Instruction:				
Special.	4,530,786	4,504,257	4,076,950	427,307
Support Services:				
Pupil.	4,312,919	4,336,085	3,887,555	448,530
Instructional staff	6,211,331	6,252,366	5,909,702	342,664
Board of education	84,625	99,625	90,917	8,708
Administration.	502,274	501,642	437,808	63,834
Fiscal	351,624	347,123	335,763	11,360
Business	219,850	191,982	180,283	11,699
Operations and maintenance.	308,545	321,964	284,953	37,011
Central.	10,000	6,650	6,650	
Facilities acquisition and construction	169,408	139,668	139,422	246
Total expenditures	<u>16,701,362</u>	<u>16,701,362</u>	<u>15,350,003</u>	<u>1,351,359</u>
Excess of revenues over (under) expenditures.	<u>(1,024,245)</u>	<u>(1,024,245)</u>	<u>450,231</u>	<u>1,474,476</u>
Other financing sources (uses):				
Refund of prior year expenditure	10,000	10,000	28,277	18,277
Refund of prior year receipts	(6,000)	(6,000)		6,000
Transfers out	(12,000)	(12,000)	(10,588)	1,412
Other miscellaneous use of funds.	(882,073)	(882,073)		882,073
Sale of capital assets.			334	334
Total other financing sources (uses)	<u>(890,073)</u>	<u>(890,073)</u>	<u>18,023</u>	<u>908,096</u>
Net change in fund balance	(1,914,318)	(1,914,318)	468,254	2,382,572
Fund balance at beginning of year.	1,840,127	1,840,127	1,840,127	
Prior year encumbrances appropriated	74,191	74,191	74,191	
Fund balance at end of year	<u><u>1,840,127</u></u>	<u><u>1,840,127</u></u>	<u><u>\$ 2,382,572</u></u>	<u><u>\$ 2,382,572</u></u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

STATEMENT OF FIDUCIARY NET ASSETS
FIDUCIARY FUNDS
JUNE 30, 2005

	Investment Trust	Agency
Assets:		
Equity in pooled cash and cash equivalents	\$ 1,123,870	\$ 820,403
Receivables:		
Accounts		78
Intergovernmental		2,320
Total assets.	1,123,870	\$ 822,801
Liabilities:		
Deposits held and due to others		\$ 822,801
Total liabilities		\$ 822,801
Net Assets:		
Net assets available for pool participants . . .	1,123,870	
Total net assets	\$ 1,123,870	

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
INVESTMENT TRUST FUND
FOR THE FISCAL YEAR ENDED JUNE 30, 2005

		<u>Investment Trust</u>
Net increase in net assets resulting from operations	\$	25,998
Distributions paid to participants.		(25,998)
Share transactions:		
Purchase of units		2,918,928
Redemptions of units.		<u>(2,820,026)</u>
Net increase in net assets and shares resulting from share transactions		<u>98,902</u>
Change in net assets		98,902
Net assets at beginning of year		<u>1,024,968</u>
Net assets at end of year	\$	<u>1,123,870</u>

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

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**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005**

NOTE 1 - DESCRIPTION OF THE ESC

The Erie-Huron-Ottawa Educational Service Center (the "ESC") is a body politic and corporate established for the purpose of exercising the rights and privileges conveyed to it by the Constitution and laws of the State of Ohio. The ESC is an Educational Service Center as defined by Section 3311.05 of the Ohio Revised Code. The ESC operates under an elected Governing Board of Education (eleven members) and is responsible for the provision of public education to residents of the local school districts that it services.

The ESC is the result of the July 1, 1997, merger of the Erie County Educational Service Center and the Ottawa County Educational Service Center, and the July 1, 1999, merger of the Erie-Ottawa Educational Service Center and the Huron County Educational Service Center, under the authority of the Ohio Revised Code Section 3311.053 and 3311.054 and resolutions made by the Governing Boards.

The ESC is staffed by 143 certified employees, 159 classified employees and 32 administrators.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The basic financial statements of the ESC have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The ESC also applies Financial Accounting Standards Board (FASB) Statements and Interpretations issued on or before November 30, 1989, to its governmental activities provided they do not conflict with or contradict GASB pronouncements. The ESC's significant accounting policies are described below.

A. Reporting Entity

The reporting entity has been defined in accordance with GASB Statement No. 14, "The Financial Reporting Entity" as amended by GASB Statement No. 39, "Determining Whether Certain Organizations Are Component Units". The reporting entity is composed of the primary government, component units and other organizations that are included to ensure that the basic financial statements of the ESC are not misleading. The primary government consists of all funds, departments, boards and agencies that are not legally separate from the ESC. For the ESC, this includes general operations, preschool and student related activities of the ESC.

Component units are legally separate organizations for which the ESC is financially accountable. The ESC is financially accountable for an organization if the ESC appoints a voting majority of the organizations' government board and (1) the ESC is able to significantly influence the programs or services performed or provided by the organization; or (2) the ESC is legally entitled to or can otherwise have access to organizations resources; or (3) the ESC is legally obligated or has otherwise assumed the responsibility to finance the deficits of, or provide financial support to, the organization; or (4) the ESC is obligated for the debt of the organization. Component units may also include organizations that are fiscally dependent on the ESC in that the ESC approves the budget, the issuance of debt or the levying of taxes. Based upon the application of these criteria, the ESC has no component units. The basic financial statements of the reporting entity include only those of the ESC (the primary government). The following organizations are described due to their relationship to the ESC:

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

JOINTLY GOVERNED ORGANIZATIONS

Bay Area Council of Governments

The Bay Area Council of Governments (BACG) is a jointly governed organization. Members of the BACG consist of 26 school districts representing 7 counties (Ottawa, Sandusky, Seneca, Erie, Huron, Wood, and Crawford). The BACG was formed for the purpose of purchasing goods and services at a lower cost. The items currently being purchased through the council of governments are natural gas and insurance. The only cost to the ESC is an administrative charge if it participates in purchasing through the BACG. The membership of BACG consists of the superintendent of each participating school district. The Board of Directors of the BACG consists of one elected representative of each county, the superintendent of the fiscal agent and two non-voting members (administrator and fiscal agent). Members of the Board serve staggered two-year terms. The ESC serves as fiscal agent for the BACG. Financial activity for fiscal 2005 is reported in the basic financial statements as an agency fund.

Northern Ohio Educational Computer Association

The Northern Ohio Educational Computer Association (NOECA) is a jointly governed organization, which is a computer consortium. NOECA is an association of 41 public school districts formed for the purpose of applying modern technology (with the aid of computers and other electronic equipment) to administrative and instructional functions among member school district. The NOECA Board of Directors consists of two representatives from each county in which participating school districts are located, the chairman of each of the operating committees, and a representative from the fiscal agent. The ESC serves as fiscal agent for NOECA. Financial activity for 2005 is reported in the basic financial statements as an investment trust fund.

PUBLIC ENTITY RISK POOLS

Ohio Association of School Business Officials Workers' Compensation Group Rating Plan

The ESC participates in a group rating plan for workers' compensation as established under Section 4123.29 of the Ohio Revised Code. The Ohio Association of School Business Officials Workers' Compensation Group Rating Plan (the "Plan") was established through the Ohio Association of School Business Officials (OASBO) as a group purchasing pool.

The Executive Director of the OASBA, or his designee, serves as coordinator of the Plan. Each year, the participating school district pays an enrollment fee to the Plan to cover the costs of administering the program

Huron-Erie School Employees Insurance Association

The Huron-Erie School Employees Insurance Association (Association) is a public entity risk pool comprised of 14 districts. The Association assembly consists of a superintendent or designated representative from each participating district and the program administrator. The Association is governed by a board of directors chosen from the general membership. The degree of control exercised by any participating district is limited to its representation on the board. Financial information can be obtained by contacting the program administrator at the Huron-Erie School Employees Insurance Association, located at 2900 Columbus Avenue, Sandusky, Ohio 44870.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

The San-Ott School Employees Welfare Benefit Association (Consortium)

The ESC participates in a shared risk pool, with participants from Sandusky and Ottawa counties. The Consortium is governed by an assembly which consists of one representative from each participant (usually the superintendent or designee). The assembly exercises control over the operation of the consortium. All consortium revenues are generated from charges for services. Financial information can be obtained by writing to San-Ott Consortium, Jay Valasek, Treasurer of Vanguard-Sentinel Vocational Schools, at 1306 Cedar Street, Fremont, Ohio 43420.

B. Fund Accounting

The ESC uses funds to maintain its financial records during the year. A fund is defined as a fiscal and accounting entity with a self balancing set of accounts. There are three categories of funds: governmental, proprietary and fiduciary. The ESC does not have any proprietary funds.

GOVERNMENTAL FUNDS

Governmental funds are those through which most governmental functions typically are financed. Governmental fund reporting focuses on the sources, uses and balances of current financial resources. Expendable assets are assigned to the various governmental funds according to the purposes for which they may or must be used. Current liabilities are assigned to the fund from which they will be paid. The difference between governmental fund assets and liabilities is reported as fund balance. The following is the ESC's major governmental fund:

General Fund - The general fund is used to account for all financial resources except those required to be accounted for in another fund. The general fund balance is available for any purpose provided it is expended or transferred according to the general laws of Ohio.

The other governmental funds of the ESC account for grants and other resources whose use is restricted to a particular purpose.

FIDUCIARY FUNDS

Fiduciary fund reporting focuses on net assets and changes in net assets. The fiduciary fund category is split into four classifications: pension trust funds, investment trust funds, private-purpose trust funds and agency funds. Trust funds are used to account for assets held by the ESC under a trust agreement for individuals, private organizations, or other governments and are therefore not available to support the ESC's own programs. The ESC's only trust fund is an investment trust fund which accounts for monies held by the ESC as fiscal agent for NOECA. Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations. The ESC's agency funds account for various resources held for other organizations and individuals.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

C. Basis of Presentation and Measurement Focus

Government-wide Financial Statements - The statement of net assets and the statement of activities display information about the ESC as a whole. These statements include the financial activities of the primary government, except for fiduciary funds.

The government-wide statement of activities presents a comparison between direct expenses and program revenues for each function or program of the governmental activities of the ESC. Direct expenses are those that are specifically associated with a service, program or department and therefore clearly identifiable to a particular function. Program revenues include amounts paid by the recipient of goods or services offered by the program and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues not classified as program revenues are presented as general revenues of the ESC.

The government-wide financial statements are prepared using the economic resources measurement focus. All assets and all liabilities associated with the operation of the ESC are included on the statement of net assets.

Fund Financial Statements - Fund financial statements report detailed information about the ESC. The focus of governmental fund financial statements is on major funds rather than reporting funds by type. Each major fund is presented in a separate column, and all nonmajor funds are aggregated into one column. Fiduciary funds are reported by fund type.

All governmental funds are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. The statement of revenues, expenditures and changes in fund balances reports on the sources (i.e., revenues and other financing sources) and uses (i.e., expenditures and other financing uses) of current financial resources. This approach differs from the manner in which the governmental activities of the government-wide financial statements are prepared. Governmental fund financial statements therefore include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements for governmental funds.

Fiduciary funds are reported using the economic resources measurement focus. Agency funds do not report a measurement focus as they do not report operations.

D. Basis of Accounting

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. Governmental funds use the modified accrual basis of accounting. Fiduciary funds also use the accrual basis of accounting.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

Revenues - Exchange and Non-exchange Transactions - Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, are recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenue is recorded in the fiscal year in which the resources are measurable and become available. Available means that the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year. For the ESC, available means expected to be received within sixty days of fiscal year-end.

Nonexchange transactions, in which the ESC receives value without directly giving equal value in return, include grants, entitlements and donations.

Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. 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 ESC must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the ESC on a reimbursement basis. On a modified accrual basis, revenue from nonexchange transactions must also be available before it can be recognized.

Under the modified accrual basis, the following revenue sources are considered to be both measurable and available at fiscal year-end: tuition, grants, and contract services.

Deferred Revenue - Deferred revenue arises when assets are recognized before revenue recognition criteria have been satisfied. Contractual services provided by the ESC during the fiscal year for which payment is not received in the available period. Grants and entitlements received before the eligibility requirements are met are also recorded as deferred revenue.

On governmental fund financial statements, receivables that will not be collected within the available period have also been reported as deferred revenue.

Expenses/Expenditures - On the accrual basis of accounting, expenses are recognized at the time they are incurred.

The measurement focus of governmental fund accounting is on decreases in net financial resources (expenditures) rather than expenses. Expenditures are generally recognized in the accounting period in which the related fund liability is incurred, if measurable. Allocation of cost, such as depreciation and amortization, are not recognized in governmental funds.

E. Budgets

The ESC adopts its budget on or before the start of the new fiscal year. Included in the budget are the estimated resources and expenditures for each fund. Upon review by the ESC's Governing Board, the annual appropriation resolution is adopted. The appropriations may be amended or supplemented throughout the year as circumstances warrant. All funds are appropriated. The Governing Board does not formally budget for resources estimated to be received during the fiscal year.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

APPROPRIATIONS

The annual appropriation resolution is enacted the by ESC's Governing Board at the fund, and function level of expenditures, which is the legal level of control. Prior to the passage of the annual appropriation measure, the Governing Board may pass a temporary appropriation measure to meet the ordinary expenditures of the ESC. Budgetary controls implemented by the ESC require that the total of expenditures and encumbrances may not exceed the appropriations totals at the levels of control established by the Governing Board. Any revisions that alter the total of any fund, function or object appropriations within a fund must be approved by the Governing Board. During the year, several supplemental appropriation measures were enacted. The Treasurer has been authorized to allocate appropriations within the object level of all funds.

The amounts reported as original budget in the budgetary statement reflects the first appropriation for that fund covering the entire fiscal year, including amounts automatically carried over from prior years. The amounts reported as the final budget represent the final appropriation the Board passed during the year.

Encumbrance accounting, under which purchase orders, contracts, and other commitments for the expenditure of monies are recorded in order to reserve that portion of the applicable appropriation, is employed as an extension of formal budgetary control in the appropriated governmental funds. Encumbrances outstanding at year-end are reported as reservations of fund balance for subsequent year expenditures on the modified accrual basis of accounting compared to encumbrances outstanding at year-end reported as expenditures on the budget basis of accounting. Note 13 provides a reconciliation of the budgetary and GAAP basis of accounting.

Formal budgetary integration is employed as a management control device during the year for all funds.

F. Cash and Investments

To improve cash management, cash received by the ESC is pooled in a central bank account. Monies for all funds are maintained in this pool. Individual fund integrity is maintained through the ESC's records. Each fund's interest in the pool is presented as "Equity in Pooled Cash and Cash Equivalents" on the financial statements.

During fiscal year 2005, investments were limited to investments in the State Treasury Asset Reserve of Ohio (STAR Ohio). STAR Ohio is an investment pool managed by the State Treasurer's Office, which allows governments within the state to pool their funds for investment purposes. STAR Ohio is not registered with the SEC as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in STAR Ohio are valued at STAR Ohio's share price which is the price the investment could be sold for on June 30, 2005.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

Under existing Ohio statutes all investment earning are assigned to the general fund unless statutorily required to be credited to a specific fund. The Board of Education has, by resolution, specified the funds to receive an allocation of interest earnings. Interest revenue credited to the general fund during fiscal year 2005 amounted to \$69,024, which includes \$25,938 assigned from other ESC funds.

For presentation on the basic financial statements, investments of the cash management pool and investments with original maturities of three months or less at the time they are purchased by the ESC are considered to be cash equivalents. Investments with an initial maturity of more than three months are reported as investments.

An analysis of the ESC's investment account at fiscal year-end is provided in Note 4.

G. Capital Assets

General capital assets are those assets specifically related to governmental activities. These assets generally result from expenditures in the governmental funds. These assets are reported in the governmental activities column of the government-wide statement of net assets but are not reported in the fund financial statements.

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 ESC maintains a capitalization threshold of five hundred dollars. The ESC 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 lives of the related capital assets. Depreciation is computed using the straight-line method over the following useful lives:

<u>Description</u>	<u>Governmental Activities Estimated Lives</u>
Building/improvements	30 - 50 years
Furniture and equipment	5 - 20 years
Vehicles	6 - 10 years

H. Compensated Absences

Compensated absences of the ESC consist of vacation leave and sick leave to the extent that payment to the employee for these absences are attributable to services already rendered and are not contingent on a specific event that is outside the control of the ESC and the employee.

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
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(Continued)**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

In accordance with the provisions of GASB Statement No. 16, "Accounting for Compensated Absences", a liability for vacation leave is accrued if (a) the employees' rights to payment are attributable to services already rendered; and (b) it is probable that the employer will compensate the employees for the benefits through paid time off or other means, such as cash payment at termination or retirement. A liability for severance is based on the sick leave accumulated at the balance sheet date by those employees who are currently eligible to receive termination (severance) payments, as well as those employees expected to become eligible in the future.

The entire compensated absence liability is reported on the government-wide financial statements.

For governmental fund financial statements, compensated absences are recognized as liabilities and expenditures as payments come due each period upon the occurrence of employee resignations and retirements.

I. Accrued Liabilities and Long-Term Obligations

All payables, accrued liabilities and long-term obligations are reported in the government-wide financial statements.

In general, governmental fund payables and accrued liabilities that, once incurred, are paid in a timely manner and in full from current financial resources are reported as obligations of the funds. However, compensated absences, and contractually required pension contributions that will be paid from governmental funds are reported as a liability in the fund financial statements only to the extent that they are due for payment during the current year.

J. Fund Balance Reserves

The ESC reserves those portions of fund equity which are legally segregated for a specific future use or which do not represent available expendable resources and therefore are not available for appropriation or expenditure. Unreserved fund balance indicates that portion of fund equity which is available for appropriation in future periods. Fund equity reserves have been established for encumbrances, principal endowment and prepayments.

K. Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets consist of capital assets, net of accumulated depreciation. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation or through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

The ESC applies restricted resources first when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
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(Continued)**

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – (Continued)

L. Prepayments

Certain payments to vendors reflect the costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements. These items are reported as assets on the balance sheet using the consumption method. A current asset for the prepaid amounts is recorded at the time of the purchase and the expenditure/expense is reported in the year in which services are consumed. At fiscal year-end, because prepayments are not available to finance future governmental fund expenditures, the fund balance is reserved on the fund financial statements by an amount equal to the carrying amount of the asset.

M. Estimates

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

N. Interfund Activity

Exchange transactions between funds are reported as revenues in the seller funds and as expenditures/expenses in the purchaser funds. Flows of cash or goods from one fund to another without a requirement for repayment are reported as interfund transfers. Repayments from funds responsible for particular expenditures/expenses to the funds that initially paid for them are not presented on the basic financial statements. Interfund activities between governmental funds are eliminated in the statement of activities.

O. Extraordinary and Special Items

Extraordinary items are transactions or events that are both unusual in nature and infrequent in occurrence. Special items are transactions or events that are within the control of the Governing Board and that are either unusual in nature or infrequent in occurrence. Neither type of transaction occurred during fiscal 2005.

NOTE 3 - ACCOUNTABILITY AND COMPLIANCE

A. Change in Accounting Principles

For fiscal year 2005, the ESC has implemented GASB Statement No. 40, "Deposit and Investment Risk Disclosures" and GASB Technical Bulletin 2004-2, "Recognition of Pension and Other Postemployment Benefit Expenditures/Expenses and Liabilities by Cost-Sharing Employers".

GASB Statement No. 40 establishes and modified disclosure requirements related to investment risks: credit risk (including custodial credit risk and concentrations of credit risk) and interest rate risk. This statement also establishes and modified disclosure requirements for custodial credit risk on deposits.

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
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(Continued)**

NOTE 3 - ACCOUNTABILITY AND COMPLIANCE – (Continued)

GASB Technical Bulletin No. 2004-2 addresses the amount that should be recognized as expenditure/expense and as a liability each period by employers participating in a cost-sharing multiple-employer pension and other postemployment benefit (OPEB) plans.

The implementation of GASB Statement No. 40 did not have an effect on the financial statements of the ESC, however additional note disclosure can be found in Note 4. The implementation of GASB Technical Bulletin No. 2004-2 had the following effect on the fund balances of the major and non-major funds of the ESC as they were previously reported as of June 30, 2004:

	<u>General</u>	<u>Nonmajor</u>	<u>Total</u>
Fund Balances, June 30, 2004	\$ 421,960	\$ 278,997	\$ 700,957
GASB Technical Bulletin No. 2004-2	(57,789)	(419)	(58,208)
Restated Fund Balance, June 30, 2004	\$ 364,171	\$ 278,578	\$ 642,749

B. Deficit Fund Balances

Fund balances at June 30, 2005, included the following individual fund deficits:

	<u>Deficit</u>
<u>Nonmajor Funds</u>	
Management Information Systems	\$ 21
Preschool Grant (State)	602
Entry Year Grant	15
Alternative Learning	26
Preschool Grant (Federal)	17,331

These funds complied with Ohio state law, which does not permit a cash basis deficit at year-end. The general fund is liable for any deficits in these funds and provides transfers when cash is required, not when accruals occur. The deficit fund balances results from adjustments for accrued liabilities.

NOTE 4 - DEPOSITS AND INVESTMENTS

The ESC maintains a cash and investment pool used by all funds. Each fund type's portion of this pool is displayed on the financial statements as "Equity in Pooled Cash and Cash Equivalents". Statutes require that the classification of monies held by the ESC into three categories.

Active deposits are public deposits necessary to meet current demands on the treasury. Such monies must be maintained either as cash in the ESC treasury, in commercial accounts payable or withdrawable on demand, including negotiable order of withdrawal (NOW) accounts, or in money market deposit accounts.

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

NOTE 4 - DEPOSITS AND INVESTMENTS – (Continued)

Inactive deposits are public deposits that the Governing Board has identified as not required for use within the current five year period of designation of depositories. Inactive deposits must either be evidenced by certificates of deposit maturing not later than the end of the current period of designation of depositories, or by savings or deposit accounts including, but not limited to, passbook accounts.

Interim deposits are deposits of interim monies. Interim moneys are those monies which are not needed for immediate use but which will be needed before the end of the current period of designation of depositories. Interim deposits must be evidenced by time certificates of deposit maturing not more than one year from the date of deposit or by savings or deposit accounts including passbook accounts.

Protection of ESC's deposits is provided by the Federal Deposit Insurance Corporation (FDIC), by eligible securities pledged by the financial institution as security for repayment, by surety company bonds deposited with the Treasurer by the financial institution or by a single collateral pool established by the financial institution to secure the repayment of all public monies deposited with the institution.

Interim monies to be deposited or invested in the following securities:

1. United States Treasury Notes, Bills, Bonds, or any other obligation or security issued by the United States Treasury or any other obligation guaranteed as to principal and interest by the United States;
2. Bonds, notes, debentures, or any other obligations or securities issued by any federal government agency or instrumentality, including but not limited to, the Federal National Mortgage Association, Federal Home Loan Bank, Federal Farm Credit Bank, Federal Home Loan Mortgage Corporation, Government National Mortgage Association, and Student Loan Marketing Association. All federal agency securities shall be direct issuances of federal government agencies or instrumentalities;
3. Written repurchase agreements in the securities listed above provided that the market value of the securities subject to the repurchase agreement must exceed the principal value of the agreement by at least two percent and be marked to market daily, and that the term of the agreement must not exceed thirty days;
4. Bonds and other obligations of the State of Ohio;
5. No-load money market mutual funds consisting exclusively of obligations described in division (1) or (2) of this section and repurchase agreements secured by such obligations, provided that investments in securities described in this division are made only through eligible institutions;
6. The State Treasurer's investment pool the State Treasury Asset Reserve of Ohio (STAR Ohio);

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
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(Continued)**

NOTE 4 - DEPOSITS AND INVESTMENTS – (Continued)

7. Certain banker's acceptance and commercial paper notes for a period not to exceed one hundred eighty days from the purchase date in an amount not to exceed twenty-five percent of the interim monies available for investment at any one time; and,
8. Under limited circumstances, corporate debt interests rated in either of the two highest classifications by at least two nationally recognized rating agencies.

Investments in stripped principal or interest obligations, reverse repurchase agreements and derivatives are prohibited. The issuance of taxable notes for the purpose of arbitrage, the use of leverage and short selling are also prohibited. An investment must mature within five years from the date of purchase unless matched to a specific obligation or debt of the ESC, and must be purchased with the expectation that it will be held to maturity. Investments may only be made through specified dealers and institutions. Payment for investments may be made only upon delivery of the securities representing the investments to the Treasurer or, if the securities are not represented by a certificate, upon receipt of confirmation of transfer from the custodian.

A. Cash on Hand

At year-end, the ESC had \$43 in undeposited cash on hand which is included on the financial statements of the ESC as part of "Equity in Pooled Cash and Cash Equivalents."

B. Deposits with Financial Institutions

At June 30, 2005, the carrying amount of all ESC deposits was \$(9,274). The negative carrying amount of deposits is due to the treasurer actively investing all available monies in STAR Ohio. Based on the criteria described in GASB Statement No. 40, "Deposits and Investment Risk Disclosures", as of June 30, 2005, \$357,457 of the ESC's bank balance of \$457,457 was exposed to custodial risk as discussed below, while \$100,000 was covered by Federal Deposit Insurance Corporation.

Custodial credit risk is the risk that, in the event of bank failure, the ESC's deposits may not be returned. Deposits of \$357,457 were collateralized by specific pledged collateral held at the Federal Reserve Bank in the name of the ESC. Although all State statutory requirements for the deposit of money had been followed, non-compliance with federal requirements could potentially subject the ESC to a successful claim by the FDIC. The ESC has no deposit policy for custodial credit risk beyond the requirements of State statute.

C. Investments

As of June 30, 2005, the ESC had the following investments and maturities:

<u>Investment type</u>	<u>Balance at Fair Value</u>	<u>Investment Maturity 6 months or less</u>
STAR Ohio	\$ 4,849,064	\$ 4,849,064

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
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NOTE 4 - DEPOSITS AND INVESTMENTS – (Continued)

Interest Rate Risk: The Ohio Revised Code generally limits security purchases to those that mature within five years of the settlement date. Interest rate risk arises because potential purchasers of debt securities will not agree to pay face value for those securities if interest rates subsequently increase. As a means of limiting its exposure to fair value losses arising from rising interest rates and according to state law, the ESC's investment policy limits investment portfolio maturities to five years or less.

Credit Risk: Standard & Poor's has assigned STAR Ohio an AAAM money market rating. Ohio law requires that STAR Ohio maintain the highest rating provided by at least one nationally recognized standard rating service.

Concentration of Credit Risk: The ESC's investment policy places no limit on the amount that may be invested in any one issuer. The following table includes the percentage of each investment type held by the ESC at June 30, 2005:

<u>Investment type</u>	<u>Fair Value</u>	<u>% of Total</u>
STAR Ohio	\$ <u>4,849,064</u>	<u>100.00%</u>

D. Reconciliation of Cash and Investment to the Statement of Net Assets

The following is a reconciliation of cash and investments as reported in the footnote above to cash and investments as reported on the statement of net assets as of June 30, 2005:

<u>Cash and Investments per footnote</u>	
Carrying amount of deposits	\$ (9,274)
Investments	4,849,064
Cash on hand	<u>43</u>
Total	<u>\$ 4,839,833</u>
 <u>Cash and investments per Statement of Net Assets</u>	
Governmental activities	\$ 2,895,560
Investment Trust	1,123,870
Agency funds	<u>820,403</u>
Total	<u>\$ 4,839,833</u>

NOTE 5 - INTERFUND TRANSACTIONS

Interfund transfers for the year ended June 30, 2005, consisted of the following, as reported on the fund financial statements:

Transfers to Nonmajor Governmental funds from:	
General Fund	\$ 10,588

All transfers made in fiscal year 2005 were in accordance with Ohio Revised Code Sections 5705.14, 5705.15 and 5705.16.

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(Continued)**

NOTE 5 - INTERFUND TRANSACTIONS – (Continued)

Transfers are used to (1) move revenues from the fund that statute or budget requires to collect them to the fund that statute or budget requires to expend them, and (2) use unrestricted revenues collected in the general fund to finance various programs accounted for in other funds in accordance with budgetary authorizations.

Interfund transfers between governmental funds are eliminated for reporting in the statement of activities.

NOTE 6 - RECEIVABLES

Receivables at June 30, 2005, consisted of intergovernmental (billings to School Districts for user charged services) and accounts (charges for individual tuition on other services). All receivables are considered collectible in full. A summary of the principal items of receivables reported on the statement of net assets follows:

Governmental Activities:	
Intergovernmental	\$ 936,721
Accounts	6,566

Receivables have been disaggregated on the face of the basic financial statements. All receivables are expected to be collected within the subsequent year.

NOTE 7 – STATE FUNDING

The Educational Service Center, under State law, provides supervisory services to the local school districts within its territory. Each city and exempted village school district that entered into an agreement with the Educational Service Center is considered to be provided supervisory services. The cost of the supervisory services is determined by HB 140. The State Department of Education apportions the costs for all supervisory services among the Educational Service Center's school districts based on each school district's total student count. The State Department of Education deducts each school district's amount from their State Foundation Program settlements and remits the amount to the Educational Service Center. The Educational Service Center may provide additional supervisory services if the majority of the school districts agree to the services and the apportionment of the costs.

The Educational Service Center also receives funding from the State Department of Education, in the amount of \$40.52 multiplied by the average daily membership of the Educational Service Center. Average daily membership includes the total student counts of all of the local school districts served by the Educational Service Center. This amount is paid from State resources. The State Department of Education also deducts from the State Foundation Program settlement of each of the school districts served by the Education Service Center an amount equal to \$6.50 for Huron and Ottawa County and \$9.50 for Erie County school districts multiplied by the school districts total student count and remits this amount to the Educational Service Center.

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
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(Continued)**

NOTE 8 - CAPITAL ASSETS

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

	<u>Balance 06/30/04</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance 06/30/05</u>
<i>Capital assets, being depreciated:</i>				
Buildings	\$ 90,000			\$ 90,000
Furniture and equipment	885,915	\$ 39,062	\$ (38,365)	886,612
Vehicles	58,439			58,439
Total capital assets, being depreciated	<u>1,034,354</u>	<u>39,062</u>	<u>(38,365)</u>	<u>1,035,051</u>
<i>Less: accumulated depreciation</i>				
Buildings	(9,300)	(1,800)		(11,100)
Furniture and equipment	(549,089)	(93,478)	37,649	(604,918)
Vehicles	(44,248)	(5,515)		(49,763)
Total accumulated depreciation	<u>(602,637)</u>	<u>(100,793)</u>	<u>37,649</u>	<u>(665,781)</u>
Governmental activities capital assets, net	<u>\$ 431,717</u>	<u>\$ (61,731)</u>	<u>\$ (716)</u>	<u>\$ 369,270</u>

Depreciation expense was charged to governmental functions as follows:

<u>Instruction:</u>	
Regular	\$ 3,959
Special	21,595
<u>Support Services:</u>	
Pupil	7,614
Instructional staff	40,065
Administration	6,300
Fiscal	1,652
Business	13,813
Operations and maintenance	4,637
Pupil Transportation	<u>1,158</u>
Total depreciation expense	<u>\$ 100,793</u>

NOTE 9 - LONG-TERM OBLIGATIONS

The ESC's long-term obligations at fiscal year-end consist of the following:

	<u>Balance Outstanding 06/30/04</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance Outstanding 06/30/05</u>	<u>Amounts Due in One Year</u>
Compensated absences	\$ 1,042,535	\$ 380,179	\$ (195,255)	\$ 1,227,459	\$ 226,704
Total	<u>\$ 1,042,535</u>	<u>\$ 380,179</u>	<u>\$ (195,255)</u>	<u>\$ 1,227,459</u>	<u>\$ 226,704</u>

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NOTE 9 - LONG-TERM OBLIGATIONS – (Continued)

Compensated absences will be paid from the fund from which the employee's salaries are paid.

NOTE 10 - RISK MANAGEMENT

A. The ESC 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 ESC has contracted with various insurance commercial carriers to provide insurance coverage for the following risks:

- Commercial property.
- Inland marine.
- Business liability.
- Business personal property.
- Business auto.
- Education liability.

Settled claims have not exceeded this commercial coverage in any of the past three years. There has been no significant reduction in coverage from the prior year.

B. Employee Health Benefits

The ESC provides employee health care benefits through the Huron-Erie School Employees Insurance Association. However, employees originally employed by the former Ottawa County Educational Service Center have benefits provided through the San-Ott School Employees Welfare Benefit Association.

The ESC has contracted with the Huron-Erie School Employees Insurance Association (Association) to provide medical/surgical, dental, vision, and life insurance benefits for its employees and their covered dependents. The Association is a shared risk pool comprised of 14 school districts that provide public education within Erie and Huron Counties. The ESC's pay monthly contributions that are placed in a common fund from which eligible claims and expenses are paid for employees of participating school districts and their covered dependents. Claims are paid for all participants regardless of claims flow.

In the event of withdrawal, the ESC shall assume and be responsible for payment of all claims of its eligible employees, families, and dependents from the effective date of withdrawal, regardless of when such claims were incurred, processed, or presented to the Association, insurance provider, insurance consultant, or any other appropriate or authorized person or representative; provided further, any such claims, which are paid after the effective date of withdrawal by the Association insurance provider or insurance consultant, or charged to such parties, shall be reimbursed in full by any withdrawing member upon demand of the Association.

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**NOTES TO THE BASIC FINANCIAL STATEMENTS
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(Continued)**

NOTE 10 - RISK MANAGEMENT – (Continued)

The ESC has contracted with the San-Ott Schools Employee Welfare Benefit Association (the "Association"), to provide medical/surgical, dental and life insurance benefits for the eligible employees employed by the former Ottawa County Educational Service Center and their dependents. The ESC pays premiums to the Association based upon the benefits structure selected. The Association Trust Agreement provides that the Association will be self-sustaining through member premiums and will reinsure through commercial companies for specific claims in excess of \$100,000 and aggregate claims in excess of 120 percent of expected claims.

C. Workers' Compensation Group Rating Plan

The ESC participates in the Ohio Association of School Business Officials Workers' Compensation Group Rating Plan (the "Plan"), an insurance purchasing pool (Note 2.A.). The intent of the Plan is to achieve the benefit of a reduced premium for the ESC by virtue of its grouping and representation with other participants in the Plan. Participants in the Plan are placed on tiers according to their loss history. Participants with low loss histories are rewarded with greater savings than participants with higher loss histories. Each participant pays its workers' compensation premium to the state based on the rate for its Plan tier rather than its individual rate. Participation in the Plan is limited to school districts that can meet the Plan's selection criteria. The firm of Sheakley UniService, Inc. provides administrative, cost control, assistance with safety programs, and actuarial services to the Plan.

NOTE 11 - DEFINED BENEFIT PENSION PLAN

A. School Employees Retirement System

The ESC contributes to the School Employees Retirement System of Ohio (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. The report may be obtained by writing to the School Employees Retirement System, 300 East Broad Street, Suite 100, Columbus, Ohio 43215-3746, or by calling toll free (800) 878-5853. It is also posted on SERS' website, www.ohsers.org; under forms and publications.

Plan members are required to contribute 10% of their annual covered salary and the ESC is required to contribute at an actuarially determined rate. The current ESC rate is 14% of annual covered payroll. A portion of the ESC's contribution is used to fund pension obligations with the remainder being used to fund health care benefits. For fiscal year 2005, 10.57% of annual covered salary was the portion used to fund pension obligations. For fiscal year 2004, 9.09% 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 a statutory maximum amount, by the SERS' Retirement Board. The adequacy of the contribution rates is determined annually. The ESC's contributions for pension obligations to SERS for the fiscal years ended June 30, 2005, 2004, and 2003, were \$401,658, \$345,812, and \$332,117, respectively; 100% has been contributed for 2005, 2004 and 2003.

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NOTE 11 - DEFINED BENEFIT PENSION PLAN – (Continued)

B. State Teachers Retirement System

The ESC contributes to the State Teachers Retirement System of Ohio (STRS), a cost-sharing, multiple-employer public employee retirement system administered by the State Teachers Retirement Board. STRS provides retirement and disability benefits, annual cost-of-living adjustments, and death and survivor benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by Chapter 3307 of the Ohio Revised Code. STRS issues a publicly available, stand-alone financial report that includes financial statements and required supplementary information. The report may be obtained by writing to the State Teachers Retirement System, 275 East Broad Street, Columbus, Ohio 43215-3371, by calling (614) 227-4090, or by visiting the STRS website at www.strsoh.org.

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% 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. 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.

Plan members are required to contribute 10% of their annual covered salary and the ESC is required to contribute at an actuarially determined rate. The current ESC rate is 14% of annual covered payroll. A portion of the ESC's contribution is used to fund pension obligations with the remainder being used to fund health care benefits. For fiscal years 2005 and 2004, 13% of annual covered salary 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% for members and 14% for employers. Chapter 3307 of the Ohio Revised Code provides statutory authority for member and employee contributions. The ESC's contributions for pension obligations to STRS for the fiscal years ended June 2005, 2004, and 2003 were \$1,083,003, \$1,106,440, \$1,168,322, respectively; 100% has been contributed for 2005, 2004, and 2003. contributions to the DC and Combined Plans for fiscal 2005 were \$6,727 made by the ESC and \$20,455 made by plan members.

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NOTE 11 - DEFINED BENEFIT PENSION PLAN – (Continued)

C. Social Security System

Effective July 1, 1991, all employees not otherwise covered by SERS or the STRS have an option to choose Social Security or the SERS/STRS. As of June 30, 2005, certain members of the Board of Education have elected Social Security. The ESC's liability is 6.2% of wages paid.

NOTE 12 - POSTEMPLOYMENT BENEFITS

The ESC provides comprehensive health care benefits to retired teachers and their dependents through STRS, and to retired non-certified employees and their dependents through SERS. Benefits include hospitalization, physicians' fees, prescription drugs, and partial reimbursement of monthly Medicare Part B premiums. Benefit provisions and the obligations to contribute are established by STRS and SERS based on authority granted by state statute. Both STRS and SERS are funded on a pay-as-you-go-basis.

The State Teachers Retirement Board has statutory authority over how much, if any, of the health care costs will be absorbed by STRS. Most benefit recipients pay a portion of the health care cost in the form of a monthly premium. By Ohio law, the cost of coverage paid from STRS funds shall be included in the employer contribution rate, currently 14% of covered payroll. For fiscal years ended June 30, 2005, and June 30, 2004, the State Teachers Retirement Board allocated employer contributions equal to 1% of covered payroll to the Health Care Stabilization Fund. For the ESC, this amount equaled \$83,272 during fiscal 2005.

STRS pays health care benefits from the Health Care Stabilization Fund. The balance in the Health Care Stabilization Fund was \$3.3 billion at June 30, 2005. For the fiscal year ended June 30, 2005, net health care costs paid by STRS were \$254.780 million and STRS had 115,395 eligible benefit recipients.

For SERS, coverage is made available to service retirees with 10 or more years of qualifying service credit, and disability and survivor benefit recipients. Effective January 1, 2004, all retirees and beneficiaries are required to pay a portion of their health care premium. The portion is based on years of service, Medicare eligibility and retirement status. A safety net is in place for retirees whose household income falls below federal poverty levels. Premiums are reduced by 50% for those who apply.

For fiscal year 2005, employer contributions to fund health care benefits were 3.43% of covered payroll. In addition, SERS levies a surcharge to fund health care benefits equal to 14% 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 has been established at \$27,400. The surcharge, added to the unallocated portion of the 14% employer contribution rate, provides for maintenance of the asset target level for the health care fund.

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FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

NOTE 12 - POSTEMPLOYMENT BENEFITS – (Continued)

The target level for the health care reserve is 150% of annual health care expenses, before premium deduction. Gross expenses for health care at June 30, 2005, were \$178.221 million and the target level is 150% of the projected claims less premium contributions for the next fiscal year. At June 30, 2005, SERS had net assets available for payment of health care benefits of \$267.5 million and SERS had approximately 58,123 participants receiving health care benefits. For the ESC, the amount to fund health care benefits, including surcharge, equaled \$144,600 during the 2005 fiscal year.

NOTE 13 - BUDGETARY BASIS OF ACCOUNTING

While reporting financial position, results of operations, and changes in fund balance on the basis of generally accepted accounting principles (GAAP), the budgetary basis as provided by law is based upon accounting for certain transactions on a basis of cash receipts and disbursements.

The Statement of Revenue, Expenditures, and Changes in Fund Balance - Budget and Actual (Non-GAAP Budgetary Basis) presented for the general fund is presented on the budgetary basis to provide a meaningful comparison of actual results with the budget. The major differences between the budget basis and the GAAP basis are that:

- (a) Revenues and other financing sources are recorded when received in cash (budget basis) as opposed to when susceptible to accrual (GAAP basis);
- (b) Expenditures and other financing uses are recorded when paid in cash (budget basis) as opposed to when the liability is incurred (GAAP basis);
- (c) In order to determine compliance with Ohio law, and to reserve that portion of the applicable appropriation, total outstanding encumbrances (budget basis) are recorded as the equivalent of an expenditure, as opposed to a reservation of fund balance for that portion of outstanding encumbrances not already recognized as an account payable (GAAP basis).

The adjustments necessary to convert the results of operations for the year on the budget basis to the GAAP basis for the general fund is as follows:

Net Change in Fund Balance		<u>General Fund</u>
Budget basis		\$ 468,254
Net adjustment for revenue accruals		86,114
Net adjustment for expenditure accruals		95,813
Net adjustment for other sources/uses		(28,277)
Adjustment for encumbrances		<u>149,656</u>
GAAP basis		<u>\$ 771,560</u>

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

NOTE 14 - CONTINGENCIES

A. Grants

The ESC receives significant financial assistance from numerous federal, state and local 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 are subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the ESC. However in the opinion of management, any such disallowed claims will not have a material effect on the financial position of the ESC.

B. Litigation

The ESC is not a party to legal proceedings that would have a material effect, if any, on the financial condition of the ESC.

C. State School Funding Decision

On December 11, 2002, the Ohio Supreme Court issued its latest opinion regarding the state's school funding plan. The decision reaffirmed earlier decisions that Ohio's current school funding plan is unconstitutional.

The Supreme Court relinquished jurisdiction over the case and directed "...the Ohio General Assembly to enact a school funding scheme that is thorough and efficient...". The ESC is currently unable to determine what effect, if any, this decision will have on its future state funding and its financial operations.

NOTE 15 - EXTERNAL INVESTMENT POOL

The ESC serves as fiscal agent for Northern Ohio Educational Association (NOECA) which is a legally separate entity. The ESC pools the monies of NOECA with the ESC's for investment purposes. Investments are not specifically purchased in the name of NOECA. The investment pool is not registered with the SEC as an investment company. The fair value of investments is determined annually. NOECA is allocated a pro rata share of each investment at fair value along with a pro rata share of the interest that it earns based upon its fund balance to the entire ESC's fund balance.

During fiscal 2005, investments of the ESC were limited to investments in STAR Ohio. The investment in STAR Ohio is valued at amounts reported by the State Treasurer and is an unclassified investment since it is not evidenced by securities that exist in physical or book entry form.

The statement of net assets and statement of changes in net assets for the external investment trust fund has been reported in the basic financial statements. Condensed financial information for the ESC's investment pool follows:

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2005
(Continued)**

NOTE 15 - EXTERNAL INVESTMENT POOL – (Continued)

Statement of Net Assets
June 30, 2005

Assets	
Equity in Pooled Cash and Cash Equivalents	\$ 4,839,833
<i>Total Assets</i>	<u>4,839,833</u>
Net Assets Held in Trust for Pool Participants	
Internal Portion	3,715,963
External Portion	<u>1,123,870</u>
<i>Total Net Assets Held in Trust for Pool Participants</i>	<u>4,839,833</u>

Statement of Changes in Net Assets
For Fiscal Year Ended June 30, 2005

Additions	
Interest	\$ 95,530
Net Capital Transactions	<u>354,939</u>
<i>Total Additions</i>	450,469
Deductions	
Distributions to Participants	<u>95,530</u>
<i>Change in Net Assets</i>	354,939
<i>Net Assets, Beginning of Year</i>	<u>4,484,894</u>
<i>Net Assets, End of Year</i>	<u>\$ 4,839,833</u>

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**SCHEDULE OF FEDERAL AWARDS EXPENDITURES
FOR THE YEAR ENDED JUNE 30, 2005**

Federal Grantor/ Pass Through Grantor Program Title	Pass Through Entity Number	Federal CFDA Number	Receipts	Disbursements
<u>U.S. DEPARTMENT OF EDUCATION</u>				
<i>Passed Through Ohio Department of Education: Special Education Cluster:</i>				
Title VI-B, Special Education Grants to States	125690-6BS3-2005	84.027	\$ 10,000	\$ 2,528
Pre-School Grant	125690-PGS1-2005	84.173	<u>83,736</u>	<u>83,736</u>
Total Special Education Cluster			<u>93,736</u>	<u>86,264</u>
Even Start	125690-EVS1-04 125690-EVS1-04	84.213	<u>205,682</u>	<u>1,616 202,568</u>
Total - Even Start			<u>205,682</u>	<u>204,184</u>
Safe and Drug-Free Schools and Communities - State Grants	125690-T4S1-2004	84.184c	<u>2,073</u>	<u>2,527</u>
Total Department of Education			<u>301,491</u>	<u>292,975</u>
<u>U. S. DEPARTMENT OF HEALTH AND HUMAN SERVICES</u>				
<i>Passed Through Ohio Department of Mental Retardation and Developmental Disabilities</i>				
Title XIX (Medicaid)		93.778	922,056	922,056
State Childrens Health Insurance Program		93.767	<u>88,462</u>	<u>88,462</u>
Total Department of Health and Human Services			<u>1,010,518</u>	<u>1,010,518</u>
Total Federal Financial Assistance			<u>\$ 1,312,009</u>	<u>\$ 1,303,493</u>

The accompanying notes to this schedule are an integral part of this schedule.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**NOTES TO THE FEDERAL AWARDS EXPENDITURES SCHEDULE
FISCAL YEAR ENDED JUNE 30, 2005**

NOTE A - SIGNIFICANT ACCOUNTING POLICIES

The accompanying Federal Awards Expenditures Schedule (the Schedule) summarizes activity of the Service Center's federal award programs. The schedule has been prepared on the cash basis of accounting.

NOTE B - MATCHING REQUIREMENTS

Certain Federal programs require that the Service Center contribute non-Federal funds (matching funds) to support the Federally-funded programs. The Service Center has complied with the matching requirements. The expenditure of non-Federal matching funds is not included on the Schedule.



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*

Erie-Huron-Ottawa Educational Service Center
Erie County
2900 Columbus Avenue
Sandusky, Ohio 44870-5569

To the Governing Board:

We have audited the financial statements of the governmental activities, the major fund, and the aggregate remaining fund information of the Erie-Huron-Ottawa Educational Service Center, Erie County (the Service Center) as of and for the year ended June 30, 2005, which collectively comprise the Service Center's basic financial statements and have issued our report thereon dated May 8, 2006, wherein we noted the Service Center adopted Governmental Accounting Standards Board Statement 40 and GASB Technical Bulletin 2004-2. 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 Service Center's internal control over financial reporting to determine our auditing procedures in order to express our opinions 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 Service Center's management dated May 8, 2006, we reported another matter involving internal control over financial reporting we did not deem a reportable condition.

Compliance and Other Matters

As part of reasonably assuring whether the Service Center'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*.

One Government Center / Room 1420 / Toledo, OH 43604-2246
Telephone: (419) 245-2811 (800) 443-9276 Fax: (419) 245-2484
www.auditor.state.oh.us

We intend this report solely for the information and use of the audit committee, management, the Governing Board, federal awarding agencies, and pass-through entities. 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

May 8, 2006



**Auditor of State
Betty Montgomery**

**INDEPENDENT ACCOUNTANTS' REPORT ON COMPLIANCE WITH REQUIREMENTS
APPLICABLE TO EACH MAJOR FEDERAL PROGRAM AND ON INTERNAL CONTROL OVER
COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

Erie-Huron-Ottawa Educational Service Center
Erie County
2900 Columbus Avenue
Sandusky, Ohio 44870-5569

To the Governing Board:

Compliance

We have audited the compliance of the Erie-Huron-Ottawa Educational Service Center, Erie County (the Service Center) with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133, Compliance Supplement that apply to its major federal program for the year ended June 30, 2005. The summary of auditor's results section of the accompanying schedule of findings identifies the Service Center's major federal program. The Service Center's management is responsible for complying with the requirements of laws, regulations, contracts, and grants applicable to each major federal program. Our responsibility is to express an opinion on the Service Center's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to reasonably assure whether noncompliance occurred with the types of compliance requirements referred to above that could directly and materially affect a major federal program. An audit includes examining, on a test basis, evidence about the Service Center's compliance with those requirements and performing other procedures we considered necessary in the circumstances. We believe our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Service Center's compliance with those requirements.

In our opinion, the Erie-Huron-Ottawa Educational Service Center, Erie County, complied, in all material respects, with the requirements referred to above that apply to its major federal program for the year ended June 30, 2005.

Internal Control Over Compliance

The Service Center's management is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the Service Center's internal control over compliance with requirements that could directly and materially affect a major federal program to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control 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 noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be timely detected by employees when performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

We intend this report solely for the information and use of the audit committee, management, the Governing Board, federal awarding agencies, and pass-through entities. It is not intended for anyone other than these specified parties.



Betty Montgomery
Auditor of State

May 8, 2006

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
ERIE COUNTY**

**SCHEDULE OF FINDINGS
OMB CIRCULAR A -133 § .505
JUNE 30, 2005**

1. SUMMARY OF AUDITOR'S RESULTS

<i>(d)(1)(i)</i>	Type of Financial Statement Opinion	Unqualified
<i>(d)(1)(ii)</i>	Were there any material control weakness conditions reported at the financial statement level (GAGAS)?	No
<i>(d)(1)(ii)</i>	Were there any other reportable control weakness conditions reported at the financial statement level (GAGAS)?	No
<i>(d)(1)(iii)</i>	Was there any reported material noncompliance at the financial statement level (GAGAS)?	No
<i>(d)(1)(iv)</i>	Were there any material internal control weakness conditions reported for major federal programs?	No
<i>(d)(1)(iv)</i>	Were there any other reportable internal control weakness conditions reported for major federal programs?	No
<i>(d)(1)(v)</i>	Type of Major Programs' Compliance Opinion	Unqualified
<i>(d)(1)(vi)</i>	Are there any reportable findings under § .510?	No
<i>(d)(1)(vii)</i>	Major Programs (list):	Title XX Medical Assistance (CFDA #93.778)
<i>(d)(1)(viii)</i>	Dollar Threshold: Type A\B Programs	Type A: > \$ 300,000 Type B: all others
<i>(d)(1)(ix)</i>	Low Risk Auditee?	Yes

**2. FINDINGS RELATED TO THE FINANCIAL STATEMENTS
REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS**

None

3. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS

None



**Auditor of State
Betty Montgomery**

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ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER

ERIE 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
MAY 30, 2006**