

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

SINGLE AUDIT

FOR THE YEAR ENDED JUNE 30, 2006



Mary Taylor, CPA
Auditor of State

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

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Mary Taylor, CPA

Auditor of State

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 ESC), as of and for the year ended June 30, 2006, which collectively comprise the ESC's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the ESC'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, 2006, and the respective changes in financial position, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 30, 2007, on our consideration of the ESC'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.

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The 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 Educational Service Center's basic financial statements. The budgetary comparison for the General Fund provides additional information and is not a required part of the basic financial statements. The schedule of federal awards expenditure is required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements. We subjected the budgetary comparison for the General Fund and schedule of federal awards expenditures 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.

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

Mary Taylor, CPA
Auditor of State

March 30, 2007

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006**

The management's 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, 2006. 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 2006 are as follows:

- In total, net assets of governmental activities decreased \$31,993 which represents a 3.15% decrease from 2005.
- General revenues accounted for \$2,639,808 in revenue or 15.29% of all revenues. Program specific revenues in the form of charges for services and sales, grants and contributions accounted for \$14,619,787 or 84.71% of total revenues of \$17,259,595.
- The ESC had \$17,291,588 in expenses related to governmental activities; only \$14,619,787 of these expenses was offset by program specific charges for services, grants or contributions. General revenues supporting governmental activities (unrestricted grants and entitlements) of \$2,639,808 were not adequate to provide for these programs.
- The ESC's only major governmental fund is the general fund. The general fund had \$15,696,905 in revenues and other financing sources and \$15,278,205 in expenditures and other financing uses. During fiscal 2006, the general fund's fund balance increased \$418,700 from \$1,135,731 to \$1,554,431.

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 2006?" 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, 2006
(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

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, Bay Area Council of Governments and the Huron-Erie School Employees Insurance Association. NOECA 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 2006 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.

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

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 2006 and 2005.

	Net Assets	
	Governmental Activities 2006	Governmental Activities 2005
<u>Assets</u>		
Current and other assets	\$ 3,562,622	\$ 3,863,807
Capital assets, net	<u>312,027</u>	<u>369,270</u>
Total assets	<u>3,874,649</u>	<u>4,233,077</u>
<u>Liabilities</u>		
Current liabilities	1,662,604	1,989,898
Long-term liabilities	<u>1,228,318</u>	<u>1,227,459</u>
Total liabilities	<u>2,890,922</u>	<u>3,217,357</u>
<u>Net Assets</u>		
Invested in capital assets	312,027	369,270
Restricted	146,784	241,590
Unrestricted	<u>524,916</u>	<u>404,860</u>
Total net assets	<u>\$ 983,727</u>	<u>\$ 1,015,720</u>

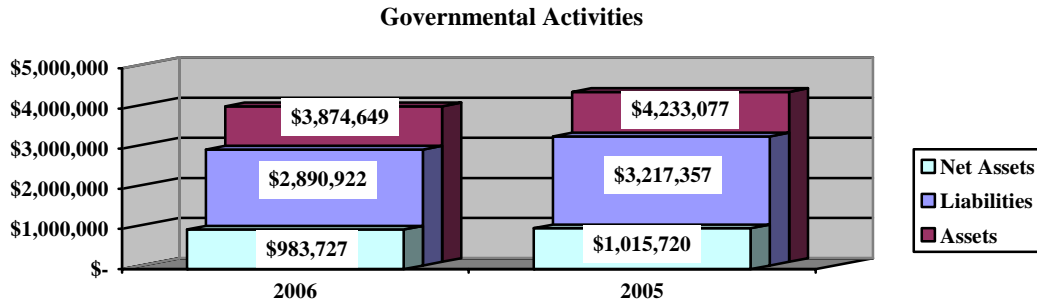
Over time, net assets can serve as a useful indicator of a government's financial position. At June 30, 2006, the ESC's assets exceeded liabilities by \$983,727. Of this total, \$146,784 is restricted in use.

At year-end, capital assets represented 8.05% of total assets. Capital assets include a building, furniture and equipment and vehicles. Capital assets, net of accumulated depreciation at June 30, 2006, were \$312,027. 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, \$146,784, represents resources that are subject to external restriction on how they may be used. The remaining balance of unrestricted net assets is \$524,916 may be used to meet the ESC's ongoing obligations to the students and creditors.

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**



The table below shows the change in net assets for fiscal year 2006 and 2005.

	Change in Net Assets	
	Governmental Activities 2006	Governmental Activities 2005
	<u>2006</u>	<u>2005</u>
<u>Revenues</u>		
Program revenues:		
Charges for services and sales	\$ 12,973,080	\$ 13,074,688
Operating grants and contributions	1,646,707	1,915,630
General revenues:		
Grants and entitlements	2,401,581	2,820,433
Investment earnings	165,093	69,532
Other	73,134	636
Total revenues	<u>17,259,595</u>	<u>17,880,919</u>

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

	Change in Net Assets	
	Governmental Activities 2006	Governmental Activities 2005
<u>Expenses</u>		
Program expenses:		
Instruction:		
Regular	\$ 94,085	\$ 70,655
Special	5,489,829	5,064,174
Support services:		
Pupil	3,693,206	3,932,649
Instructional staff	5,928,898	6,326,864
Board of education	55,147	88,968
Administration	775,310	715,507
Fiscal	341,060	362,987
Business	211,154	202,743
Operations and maintenance	447,122	395,811
Pupil transportation	1,158	271
Central	151,107	90,463
Operations of non-instructional services	24,373	47,132
Extracurricular activities	6,254	6,618
Intergovernmental	72,885	40,426
Total expenses	17,291,588	17,345,268
Change in net assets	(31,993)	535,651
Net assets at beginning of year	1,015,720	480,069
Net assets at end of year	<u>\$ 983,727</u>	<u>\$ 1,015,720</u>

Governmental Activities

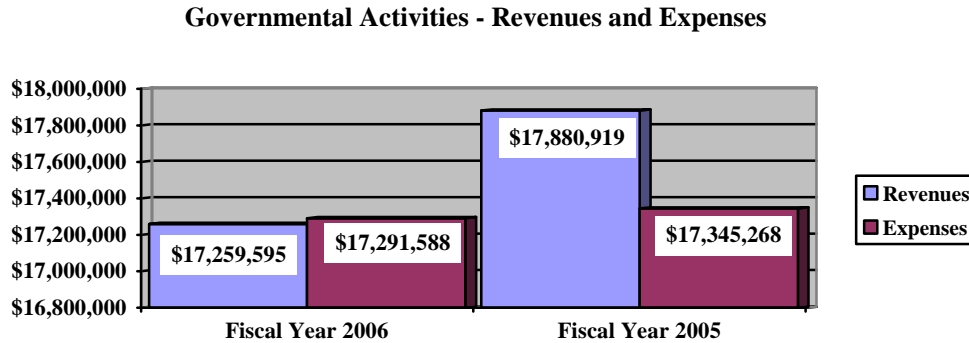
Net assets of the ESC's governmental activities decreased \$31,993. Total governmental expenses of \$17,291,588 were not completely offset by program revenues of \$14,619,787 and general revenues of \$2,639,808. Program revenues supported 84.55% of the total governmental expenses.

The primary sources of revenue for governmental activities are derived from contracted fees for services provided to other entities. This revenue source represents 75.16% of total governmental revenue.

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

The graph below presents the ESC's governmental activities revenue and expenses for fiscal years 2006 and 2005.



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

	Total Cost of Services <u>2006</u>	Net Cost of Services <u>2006</u>	Total Cost of Services <u>2005</u>	Net Cost of Services <u>2005</u>
Program expenses				
Instruction:				
Regular	\$ 94,085	\$ 33,902	\$ 70,655	\$ 9,672
Special	5,489,829	770,483	5,064,174	404,344
Support services:				
Pupil	3,693,206	596,596	3,932,649	643,954
Instructional staff	5,928,898	923,809	6,326,864	951,278
Board of education	55,147	9,008	88,968	14,605
Administration	775,310	113,208	715,507	66,718
Fiscal	341,060	61,973	362,987	23,331
Business	211,154	40,388	202,743	49,672
Operations and maintenance	447,122	66,812	395,811	177,876
Pupil transportation	1,158	1,158	271	271
Central	151,107	50,838	90,463	12,827
Operation of non-instructional services	24,373	16,555	47,132	(14,596)
Extracurricular activities	6,254	3,815	6,618	4,700
Intergovernmental	72,885	(16,744)	40,426	10,298
Total expenses	<u>\$ 17,291,588</u>	<u>\$ 2,671,801</u>	<u>\$ 17,345,268</u>	<u>\$ 2,354,950</u>

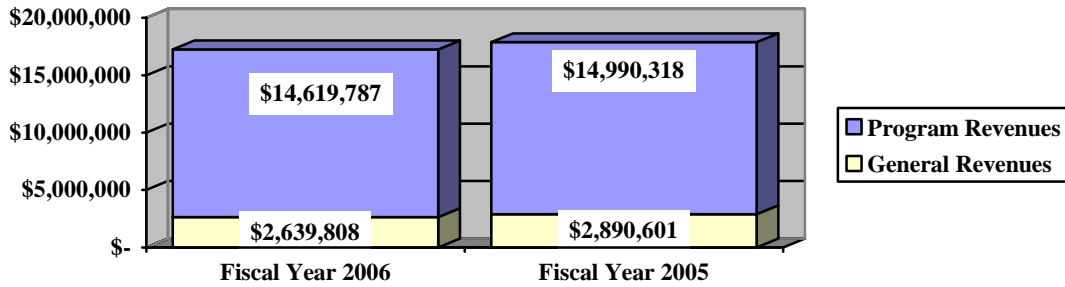
For all governmental activities, program revenue support is 84.55%. The primary support of the ESC is contracted fees for services provided to other districts.

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

The graph below presents the ESC's governmental activities revenue for fiscal year 2006 and 2005.

Governmental Activities - General and Program Revenues



The ESC's Funds

The ESC's governmental funds reported a combined fund balance of \$1,691,719, which is higher than last year's total of \$1,471,040. The schedule below indicates the fund balance and the total change in fund balance as of June 30, 2006 and 2005.

	Fund Balance June 30, 2006	Fund Balance June 30, 2005	Increase (Decrease)
General	\$ 1,554,431	\$ 1,135,731	\$ 418,700
Other Governmental	137,288	335,309	(198,021)
Total	\$ 1,691,719	\$ 1,471,040	\$ 220,679

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

General Fund

The ESC's general fund balance increased by \$418,700. 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.

	<u>2006</u> <u>Amount</u>	<u>2005</u> <u>Amount</u>	<u>Percentage</u> <u>Change</u>
<u>Revenues</u>			
Tuition	\$ 23,685	\$ 32,262	(26.59) %
Services provided to other entities	12,922,030	12,669,279	1.99 %
Earnings on investments	163,891	69,024	137.44 %
Intergovernmental	2,532,832	3,087,861	(17.97) %
Other revenues	<u>54,019</u>	<u>27,922</u>	93.46 %
Total	<u>\$ 15,696,457</u>	<u>\$ 15,886,348</u>	(1.20) %
<u>Expenditures</u>			
Instruction	\$ 4,528,865	\$ 4,066,913	11.36 %
Support services	10,599,353	10,898,849	(2.75) %
Facilities acquisition and construction	<u>144,418</u>	<u>138,772</u>	4.07 %
Total	<u>\$ 15,272,636</u>	<u>\$ 15,104,534</u>	1.11 %

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

Capital Assets

At the end of fiscal 2006, the ESC had \$312,027 invested in buildings, furniture and equipment, and vehicles. This entire amount is reported in governmental activities. The following table shows fiscal 2006 balances compared to 2005:

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

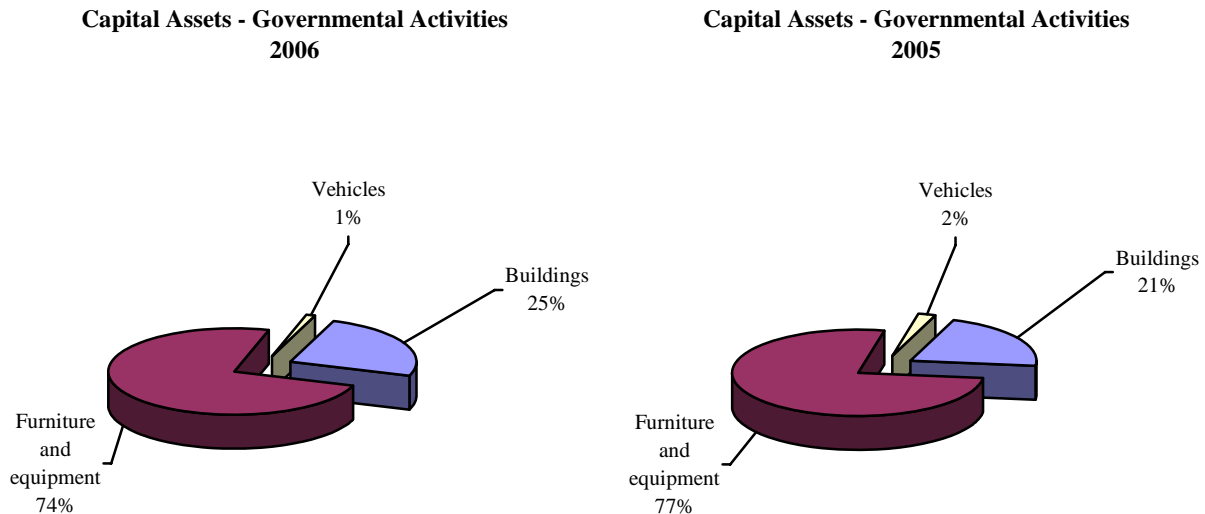
	<u>Governmental Activities</u>	
	<u>2006</u>	<u>2005</u>
Buildings	\$ 77,100	\$ 78,900
Furniture and equipment	231,766	281,694
Vehicles	<u>3,161</u>	<u>8,676</u>
Total	<u>\$ 312,027</u>	<u>\$ 369,270</u>

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

Total additions to capital assets for 2006 were \$33,672. A total of \$90,915 in depreciation expense was recognized for fiscal 2006.

The graphs below present the District's capital assets for fiscal 2006 and fiscal 2005.



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

Debt

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

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 2007 and beyond due to additional service requests from districts and also the addition of two local districts from Sandusky County (Lakota and Woodmore). 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 the Huron-Erie School Employees Insurance Consortium. 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. What effect this legislation will have on future state funding and on ESC financial operations is uncertain at this time.

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

**MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

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, 2006

	Governmental Activities
Assets:	
Equity in pooled cash and cash equivalents. . .	\$ 3,133,013
Receivables:	
Accounts	12,420
Intergovernmental	368,223
Accrued interest.	353
Prepayments.	48,613
Depreciable capital assets, net	312,027
 Total assets	 3,874,649
Liabilities:	
Accounts payable	74,090
Accrued wages and benefits	1,268,444
Pension obligation payable.	215,557
Intergovernmental payable	104,513
Long-term liabilities:	
Due within one year.	269,942
Due within more than one year	958,376
 Total liabilities	 2,890,922
Net Assets:	
Invested in capital assets	312,027
Restricted for:	
Permanent endowment	2,645
Locally funded programs.	68,108
State funded programs.	500
Federally funded programs.	74,415
Other purposes.	1,116
Unrestricted.	524,916
 Total net assets	 \$ 983,727

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, 2006

	<u>Expenses</u>	<u>Program Revenues</u>		<u>Net (Expense)</u>
		<u>Charges for Services and Sales</u>	<u>Operating Grants and Contributions</u>	<u>Revenue and Changes in Net Assets</u>
				<u>Governmental Activities</u>
Governmental activities:				
Instruction:				
Regular	\$ 94,085	\$ 37,620	\$ 22,563	\$ (33,902)
Special	5,489,829	3,806,020	913,326	(770,483)
Support services:				
Pupil.	3,693,206	2,995,203	101,407	(596,596)
Instructional staff	5,928,898	4,759,920	245,169	(923,809)
Board of education	55,147	46,139		(9,008)
Administration.	775,310	445,912	216,190	(113,208)
Fiscal.	341,060	238,421	40,666	(61,973)
Business.	211,154	170,766		(40,388)
Operations and maintenance	447,122	380,310		(66,812)
Pupil transportation.	1,158			(1,158)
Central	151,107	82,512	17,757	(50,838)
Operation of non-instructional services.	24,373	7,818		(16,555)
Extracurricular activities.	6,254	2,439		(3,815)
Intergovernmental	72,885		89,629	16,744
Total governmental activities	\$ 17,291,588	\$ 12,973,080	\$ 1,646,707	(2,671,801)

General Revenues:

Grants and entitlements not restricted to specific programs	2,401,581
Investment earnings	165,093
Miscellaneous	73,134
Total general revenues	2,639,808
Change in net assets	(31,993)
Net assets at beginning of year.	1,015,720
Net assets at end of year	\$ 983,727

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

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

BALANCE SHEET
GOVERNMENTAL FUNDS
JUNE 30, 2006

	<u>General</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Assets:			
Equity in pooled cash and cash equivalents	\$ 2,953,783	\$ 179,230	\$ 3,133,013
Receivables:			
Accounts	12,420		12,420
Intergovernmental	281,403	86,820	368,223
Accrued interest.	353		353
Prepayments	47,745	868	48,613
Total assets.	<u>\$ 3,295,704</u>	<u>\$ 266,918</u>	<u>\$ 3,562,622</u>
Liabilities:			
Accounts payable.	\$ 64,162	\$ 9,928	\$ 74,090
Accrued wages and benefits	1,251,227	17,217	1,268,444
Compensated absences payable	76,436		76,436
Pension obligation payable	211,552	4,005	215,557
Intergovernmental payable.	89,023	15,490	104,513
Deferred revenue.	48,873	82,990	131,863
Total liabilities.	<u>1,741,273</u>	<u>129,630</u>	<u>1,870,903</u>
Fund Balances:			
Reserved for encumbrances	106,362	16,847	123,209
Reserved for prepayments	47,745	868	48,613
Reserved for principal endowment.		2,645	2,645
Unreserved, undesignated, reported in:			
General fund	1,400,324		1,400,324
Special revenue funds.		116,928	116,928
Total fund balances	<u>1,554,431</u>	<u>137,288</u>	<u>1,691,719</u>
Total liabilities and fund balances.	<u>\$ 3,295,704</u>	<u>\$ 266,918</u>	<u>\$ 3,562,622</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, 2006

Total governmental fund balances		\$ 1,691,719
<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.		312,027
Other long-term assets are not available to pay for current-period expenditures and therefore are deferred in the funds.		
Accounts	\$ 12,620	
Intergovernmental	<u>119,243</u>	
Total		131,863
Long-term liabilities are not due and payable in the current period and therefore are not reported in the funds.		<u>(1,151,882)</u>
Net assets of governmental activities		<u><u>\$ 983,727</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, 2006**

	<u>General</u>	<u>Other Governmental Funds</u>	<u>Total Governmental Funds</u>
Revenues:			
From local sources:			
Services provided to other entities	\$ 12,922,030	\$ 169,882	\$ 13,091,912
Tuition	23,685		23,685
Earnings on investments	163,891	1,202	165,093
Extracurricular		6,818	6,818
Contributions and donations		17,315	17,315
Other local revenues	54,019	2,550	56,569
Intergovernmental - intermediate sources		25,200	25,200
Intergovernmental - state	2,265,759	1,255,503	3,521,262
Intergovernmental - federal	267,073	282,364	549,437
Total revenue.	<u>15,696,457</u>	<u>1,760,834</u>	<u>17,457,291</u>
Expenditures:			
Current:			
Instruction:			
Regular		79,996	79,996
Special	4,528,865	907,530	5,436,395
Support Services:			
Pupil	3,585,622	118,984	3,704,606
Instructional staff	5,598,789	342,419	5,941,208
Board of education	55,147		55,147
Administration	544,086	227,057	771,143
Fiscal	289,985	54,185	344,170
Business	203,653		203,653
Operations and maintenance	306,001		306,001
Central	16,070	135,037	151,107
Operation of non-instructional services		20,077	20,077
Extracurricular activities		6,254	6,254
Facilities acquisition and construction	144,418		144,418
Intergovernmental pass through	-	72,885	72,885
Total expenditures.	<u>15,272,636</u>	<u>1,964,424</u>	<u>17,237,060</u>
Excess of revenues over (under) expenditures.	<u>423,821</u>	<u>(203,590)</u>	<u>220,231</u>
Other financing sources (uses):			
Transfers in		5,569	5,569
Transfers out	(5,569)		(5,569)
Sale of capital assets	448		448
Total other financing sources (uses).	<u>(5,121)</u>	<u>5,569</u>	<u>448</u>
Net change in fund balances.	418,700	(198,021)	220,679
Fund balances at beginning of year.	1,135,731	335,309	1,471,040
Fund balances at end of year	<u>\$ 1,554,431</u>	<u>\$ 137,288</u>	<u>\$ 1,691,719</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, 2006

Net change in fund balances - total governmental funds \$ 220,679

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	\$ 33,672	
Current year depreciation	<u>(90,915)</u>	
Total		(57,243)

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

Intergovernmental	(508)	
Accounts receivable	<u>(190,703)</u>	
Total		(191,211)

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.		<u>(4,218)</u>
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Change in net assets of governmental activities **\$ (31,993)**

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, 2006

	Investment Trust	Agency
Assets:		
Equity in pooled cash and cash equivalents	\$ 1,541,404	\$ 4,712,402
Receivables:		
Accounts		2,885
Accrued interest.		72,926
	1,541,404	4,788,213
Total assets.	<u>1,541,404</u>	<u>\$ 4,788,213</u>
Liabilities:		
Accounts payable.		\$ 1,035,560
Due to other governments		217
Deposits held and due to others		3,752,436
		3,752,436
Total liabilities		<u>\$ 4,788,213</u>
Net Assets:		
Net assets available for pool participants	1,541,404	
Total net assets	<u>\$ 1,541,404</u>	

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, 2006

	Investment Trust
Net increase in net assets resulting from operations \$	64,059
Distributions paid to participants.	(64,059)
Share transactions:	
Purchase of units	3,427,728
Redemptions of units.	(3,010,194)
Net increase in net assets and shares resulting from share transactions	417,534
Change in net assets	417,534
Net assets at beginning of year	1,123,870
Net assets at end of year	\$ 1,541,404

SEE ACCOMPANYING NOTES TO THE BASIC FINANCIAL STATEMENTS

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

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006**

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 162 certified employees, 143 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, 2006
(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 2006 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 2006 is reported in the basic financial statements as an investment trust fund. The ESC paid NOECA \$58,704 in fiscal year 2006 for their services.

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 OASBO, 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. On January 1, 2006, the ESC became fiscal agent for the Association. Financial activity for 2006 is reported in the basic financial statements as an agency fund. This financial activity does not include federal securities for which the treasurer of the EHOVE Career Center is the custodian.

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

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

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

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.

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.

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

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

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

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.

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.

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

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

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

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. 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 2006, 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, 2006.

Under existing Ohio statutes all investment earnings are assigned to the general fund unless statutorily required to be credited to a specific fund. The Governing Board has, by resolution, specified the funds to receive an allocation of interest earnings. Interest revenue credited to the general fund during fiscal year 2006 amounted to \$163,891, which includes \$52,687 assigned from other ESC funds.

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

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

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

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.

F. 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

G. 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.

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. Sick leave benefits are accrued as a liability using the vesting method. A liability 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.

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

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

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

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.

H. 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 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.

I. 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.

J. 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.

K. 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.

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

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

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

L. 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.

M. 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.

N. 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 Board of Education and that are either unusual in nature or infrequent in occurrence. Neither type of transaction occurred during fiscal 2006.

NOTE 3 - ACCOUNTABILITY AND COMPLIANCE

A. Change in Accounting Principles

For fiscal year 2006, the ESC has implemented GASB Statement No. 42, "Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries", GASB Statement No. 46, "Net Assets Restricted by Enabling Legislation", and GASB Statement No. 47, "Accounting for Termination Benefits".

GASB Statement No. 42 amends GASB Statement No. 34 and establishes accounting and financial reporting standards for impairment of capital assets and accounting requirements for insurance recoveries.

GASB Statement No. 46 defines enabling legislation and specifies how net assets should be reported in the financial statements when there are changes in such legislation. The Statement also requires governments to disclose in the notes to the financial statements the amount of net assets restricted by enabling legislation.

GASB Statement No. 47 establishes accounting standards for termination benefits.

The implementation of GASB Statement No. 42, GASB Statement No. 46 and GASB Statement No. 47 did not have an effect on the fund balances/net assets of the ESC as previously reported at June 30, 2005.

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

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 3 - ACCOUNTABILITY AND COMPLIANCE – (Continued)

B. Deficit Fund Balances

Fund balances at June 30, 2006, included the following individual fund deficits:

<u>Nonmajor Funds</u>	<u>Deficit</u>
Management Information Systems	\$ 29
Preschool Grant (State)	2,053
Miscellaneous State Grants	680
Alternative Learning	4,636
IDEA Part B	206
Title I	8,475
Preschool Grant (Federal)	587

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 result 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.

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.

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

**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 4 - DEPOSITS AND INVESTMENTS – (Continued)

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);
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."

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 4 - DEPOSITS AND INVESTMENTS – (Continued)

B. Deposits with Financial Institutions

At June 30, 2006, the carrying amount of all ESC deposits was \$686,409. Based on the criteria described in GABB Statement No. 40, "Deposits and Investment Risk Disclosure", as of June 30, 2006, \$903,747 of the ESC's bank balance of \$1,003,747 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 a bank failure, the ESC's deposits may not be returned. Deposits of \$903,747 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 the State statute.

C. Investments

As of June 30, 2006, 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	\$ 8,700,367	\$ 8,700,367

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 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, 2006:

<u>Investment type</u>	<u>Fair Value</u>	<u>% of Total</u>
STAR Ohio	\$ 8,700,367	100.00%

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 4 - DEPOSITS AND INVESTMENTS – (Continued)

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, 2006:

<u>Cash and Investments per footnote</u>	
Carrying amount of deposits	\$ 686,409
Investments	8,700,367
Cash on hand	43
Total	<u>\$ 9,386,819</u>
 <u>Cash and investments per Statement of Net Assets</u>	
Governmental activities	\$ 3,133,013
Investment Trust	1,541,404
Agency funds	4,712,402
Total	<u>\$ 9,386,819</u>

NOTE 5 - INTERFUND TRANSACTIONS

Interfund transfers for the year ended June 30, 2006, consisted of the following, as reported on the fund financial statements:

Transfers to Nonmajor Governmental funds from:

General Fund	\$ 5,569
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All transfers made in fiscal year 2006 were in accordance with Ohio Revised Code Sections 5705.14, 5705.15 and 5705.16.

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.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 6 - RECEIVABLES

Receivables at June 30, 2006, consisted of intergovernmental (billings to School Districts for user charged services), accrued interest 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	\$ 368,223
Accounts	12,420
Accrued interest	<u>353</u>
Total	<u>\$ 380,996</u>

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 ESC, 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 ESC 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 ESC's school districts based on each school district's total count. The State Department of Education deducts each school district's amount from their State Foundation Program settlements and remits the amount to the ESC. The ESC may provide additional supervisory services if the majority of the school districts agree to the services and the apportionment of the costs.

The ESC also receives funding from the State Department of Education, in the amount of \$40.52 multiplied by the average daily membership of the ESC. Average daily membership includes the total student counts of all of the local school districts served by the ESC. 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 ESC. 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 ESC.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 8 - CAPITAL ASSETS

Capital asset activity for the fiscal year ended June 30, 2006, was as follows:

	<u>Balance 06/30/05</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance 06/30/06</u>
<i>Capital assets, being depreciated:</i>				
Buildings	\$ 90,000	\$ -	\$ -	\$ 90,000
Furniture and equipment	886,612	33,672		920,284
Vehicles	<u>58,439</u>	<u>-</u>	<u>-</u>	<u>58,439</u>
Total capital assets, being depreciated	<u>1,035,051</u>	<u>33,672</u>	<u>-</u>	<u>1,068,723</u>
<i>Less: accumulated depreciation</i>				
Buildings	(11,100)	(1,800)		(12,900)
Furniture and equipment	(604,918)	(83,600)		(688,518)
Vehicles	<u>(49,763)</u>	<u>(5,515)</u>	<u>-</u>	<u>(55,278)</u>
Total accumulated depreciation	<u>(665,781)</u>	<u>(90,915)</u>	<u>-</u>	<u>(756,696)</u>
Governmental activities capital assets, net	<u>\$ 369,270</u>	<u>\$ (57,243)</u>	<u>\$ -</u>	<u>\$ 312,027</u>

Depreciation expense was charged to governmental functions as follows:

<u>Instruction:</u>	
Regular	\$ 4,090
Special	21,161
<u>Support Services:</u>	
Pupil	7,114
Instructional staff	35,021
Administration	5,338
Fiscal	1,878
Business	10,963
Operations and maintenance	4,192
Pupil Transportation	<u>1,158</u>
Total depreciation expense	<u>\$ 90,915</u>

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 9 - LONG-TERM OBLIGATIONS

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

	Balance Outstanding <u>06/30/05</u>	<u>Additions</u>	<u>Reductions</u>	Balance Outstanding <u>06/30/06</u>	Amounts Due in <u>One Year</u>
Compensated absences	<u>\$ 1,227,459</u>	<u>\$ 282,942</u>	<u>\$ (282,083)</u>	<u>\$ 1,228,318</u>	<u>\$ 269,942</u>

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 2006, 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.

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
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 10 - RISK MANAGEMENT – (Continued)

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 - PENSION PLANS

A. School Employees Retirement System

The ESC contributes to the School Employees Retirement System (SERS), a cost-sharing multiple employer defined benefit pension plan. SERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by Chapter 3309 of the Ohio Revised Code. SERS issues a publicly available, stand-alone financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the School Employees Retirement System, 300 East Broad Street, Suite 100, Columbus, Ohio 43215-3746 or by calling (800) 878-5853. It is also posted on SERS' website, www.ohsers.org, under Forms and Publications.

Plan members are required to contribute 10 percent of their annual covered salary and the ESC is required to contribute at an actuarially determined rate. The current ESC rate is 14 percent 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 2006, 10.58 percent of annual covered salary was the portion used to fund pension obligations. For fiscal year 2005, 10.57 percent of annual covered salary was the portion used to fund pension obligations. For fiscal year 2004, 9.09 percent of annual covered salary was the portion used to fund pension obligations. The contribution requirements of plan members and employers are established and may be amended, up to statutory maximum amounts, by the SERS' Retirement Board. The ESC's required contribution for pension obligations to SERS for fiscal years ended 2006, 2005, and 2004 were \$433,208, \$401,658, and \$345,812, respectively. 100 percent has been contributed for fiscal year 2006 and 100 percent for fiscal years 2005 and 2004.

B. State Teachers Retirement System

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

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 11 - PENSION PLANS – (Continued)

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

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

For the fiscal year ended June 30, 2006, plan members were required to contribute 10 percent of their annual covered salaries. The ESC was required to contribute 14 percent; 13 percent was the portion used to fund pension obligations. Contribution rates are established by the State Teachers Retirement Board, upon recommendation of its consulting actuary, not to exceed statutory maximum rates of 10 percent for members and 14 percent for employers. Chapter 3307 of the Ohio Revised Code provides statutory authority for member and employer contributions.

The ESC's required contributions for fund pension obligations to the DB Plan for the fiscal years ended June 30, 2006, 2005, and 2004, were \$1,085,843, \$1,083,003 and \$1,106,440, respectively. 100 percent has been contributed for fiscal year 2006 and 100 percent for fiscal years 2005 and 2004. Contributions to the DC and Combined Plans for fiscal year 2006 were \$12,555 made by the ESC and \$27,946 made by the plan members.

C. Social Security System

Effective July 1, 1991, all employees not otherwise covered by the SERS or the STRS have an option to choose Social Security or the SERS/ STRS. As of June 30, 2006, certain members of the Governing Board have elected Social Security. The ESC's liability is 6.2% of wages paid.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 11 - PENSION PLANS – (Continued)

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

STRS Ohio retirees who participated in the DB or combined plans and their dependents are eligible for health care coverage. The STRS Ohio Board has statutory authority over how much, if any, of the health care costs will be absorbed by STRS Ohio. All benefit recipients pay a portion of health care cost in the form of a monthly premium. By law, the cost of coverage paid from STRS Ohio funds is included in the employer contribution rate, currently 14 percent of covered payroll. For the fiscal year ended June 30, 2006, the STRS Ohio Board allocated employer contributions equal to 1 percent of covered payroll to the Health Care Reserve Fund. For the ESC, this amount equaled \$83,526 for fiscal year 2006.

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

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

After the allocation for basic benefits, the remainder of the employer's 14 percent contribution is allocated to providing health care benefits. For the fiscal year ended June 30, 2006, employer contributions to fund health care benefits were 3.42 percent of covered payroll, a decrease of 0.01 percent from fiscal year 2005. In addition, SERS levies a surcharge to fund health care benefits equal to 14 percent of the difference between a minimum pay and the member's pay, pro-rated for partial service credit. For fiscal year 2006, the minimum pay was established at \$35,800. However, the surcharge is capped at 2 percent of each employer's SERS salaries. For the 2006 fiscal year, ESC paid \$218,572 to fund health care benefits, including the surcharge.

The surcharge, added to the unallocated portion of the 14 percent employer contribution rate, provides for maintenance of the asset target level for the health care fund. The target level for the health care reserve is 150 percent of annual health care expenses. Expenses for health care for the fiscal year ended June 30, 2005 (the latest information available) were \$178.221 million. At June 30, 2005 (the latest information available), SERS had net assets available for payment of health care benefits of \$267.5 million, which is about 168 percent of next years projected net health care costs of \$158.776 million. On the basis of actuarial projections, the allocated contributions will be insufficient in the long term, to provide for a health care reserve equal to at least 150 percent of estimated annual net claim costs. SERS has 58,123 participants currently receiving health care benefits.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 13 - 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.

NOTE 14 - 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 2006, 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.

**ERIE-HURON-OTTAWA EDUCATIONAL SERVICE CENTER
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**NOTES TO THE BASIC FINANCIAL STATEMENTS
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 14 - EXTERNAL INVESTMENT POOL - (Continued)

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:

Statement of Net Assets
June 30, 2006

Assets	
Equity in Pooled Cash and Cash Equivalents	\$ 9,386,819
Accrued interest receivable	<u>73,279</u>
<i>Total Assets</i>	<u><u>\$ 9,460,098</u></u>
Net Assets Held in Trust for Pool Participants	
Internal Portion	\$ 7,918,694
External Portion	<u>1,541,404</u>
<i>Total Net Assets Held in Trust for Pool Participants</i>	<u><u>\$ 9,460,098</u></u>

Statement of Changes in Net Assets
For Fiscal Year Ended June 30, 2006

Additions	
Interest	\$ 495,670
Net Capital Transactions	<u>4,483,389</u>
<i>Total Additions</i>	4,979,059
Deductions	
Distributions to Participants	<u>358,794</u>
<i>Change in Net Assets</i>	4,620,265
<i>Net Assets, Beginning of Year</i>	<u>4,839,833</u>
<i>Net Assets, End of Year</i>	<u><u>\$ 9,460,098</u></u>

**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, 2006**

	<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	\$ 13,545,000	\$ 13,545,000	\$ 13,215,329	\$ (329,671)
Tuition	28,000	28,000	24,185	(3,815)
Earnings on investments	73,000	73,000	163,538	90,538
Other local revenues	50,000	50,000	48,836	(1,164)
Intergovernmental - state	3,247,731	3,247,731	2,265,759	(981,972)
Intergovernmental - federal	750,000	750,000	267,073	(482,927)
Total revenue	<u>17,693,731</u>	<u>17,693,731</u>	<u>15,984,720</u>	<u>(1,709,011)</u>
Expenditures:				
Current:				
Instruction:				
Special	5,517,889	5,519,578	4,599,053	920,525
Support Services:				
Pupil	4,887,081	4,884,292	3,713,952	1,170,340
Instructional staff	7,309,094	7,298,412	5,891,265	1,407,147
Board of education	99,550	99,550	54,179	45,371
Administration	575,134	575,134	513,182	61,952
Fiscal	335,434	335,434	290,248	45,186
Business	243,114	248,774	208,819	39,955
Operations and maintenance	389,756	397,261	321,553	75,708
Central	7,050	7,050	4,590	2,460
Facilities acquisition and construction	160,918	159,535	144,418	15,117
Total expenditures	<u>19,525,020</u>	<u>19,525,020</u>	<u>15,741,259</u>	<u>3,783,761</u>
Excess of revenues over (under) expenditures	<u>(1,831,289)</u>	<u>(1,831,289)</u>	<u>243,461</u>	<u>2,074,750</u>
Other financing sources (uses):				
Refund of prior year expenditure	1,500	1,500	10,750	9,250
Transfers out	(6,000)	(6,000)	(5,569)	431
Other miscellaneous use of funds	(696,539)	(696,539)		696,539
Sale of capital assets	100	100	448	348
Total other financing sources (uses)	<u>(700,939)</u>	<u>(700,939)</u>	<u>5,629</u>	<u>706,568</u>
Net change in fund balance	(2,532,228)	(2,532,228)	249,090	2,781,318
Fund balance at beginning of year	2,382,572	2,382,572	2,382,572	2,382,572
Prior year encumbrances appropriated	149,656	149,656	149,656	149,656
Fund balance at end of year	\$ -	\$ -	\$ 2,781,318	\$ 2,781,318

SEE ACCOMPANYING NOTES TO THE SUPPLEMENTAL INFORMATION

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

**NOTES TO SUPPLEMENTAL INFORMATION
FOR THE FISCAL YEAR ENDED JUNE 30, 2006**

NOTE 1 - BUDGETARY PROCESS

There are no budgetary requirements for Educational Service Centers identified in the Ohio Revised Code nor does the State Department of Education specify any budgetary guidelines to be followed.

The Educational Service Center's Board budgets for resources estimated to be received during the fiscal year. The estimated revenues may be amended during the fiscal year if projected increases or decreases in revenue are identified by the Treasurer. The amounts reported as both the original budgeted amounts and the final budgeted amounts on the budgetary statements reflect the amounts of the estimated revenues in effect at the time final appropriations were passed by the Board.

The Educational Service Center's Board adopts an annual appropriations resolution, which is the Board's authorization to spend resources and sets annual limits on expenditures plus encumbrances at the level of control selected by the Board. The level of control has been established by the Board at the fund and function level for all funds. The Treasurer has been authorized to allocate appropriations to the function and object level within all funds.

Throughout the fiscal year, appropriations may be amended or supplemented as circumstances warrant. The amounts reported as the original budgeted amounts on the budgetary statements reflect the amounts on the first appropriations resolution for that fund that covered the entire fiscal year, including amounts automatically carried forward from prior fiscal years. The amounts reported as the final budgeted amounts on the budgetary statements represent the final appropriation amounts passed by the Board during the fiscal year.

NOTE 2- 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).

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

**NOTES TO SUPPLEMENTAL INFORMATION
FOR THE FISCAL YEAR ENDED JUNE 30, 2006
(Continued)**

NOTE 2- BUDGETARY BASIS OF ACCOUNTING – (Continued)

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	\$ 249,090
Net adjustment for revenue accruals	(288,263)
Net adjustment for expenditure accruals	296,158
Net adjustment for other sources/uses	(10,750)
Adjustment for encumbrances	<u>172,465</u>
GAAP basis	<u>\$ 418,700</u>

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

**SCHEDULE OF FEDERAL AWARDS EXPENDITURES
FOR THE YEAR ENDED JUNE 30, 2006**

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:</i>				
Special Education Cluster:				
Title VI-B, Special Education Grants to States	125690-6BS3-2005	84.027	\$ 90,000	\$ 97,472
Pre-School Grant	125690-PGS1-2005	84.173	7,293	7,293
	125690-PGS1-2006		89,629	89,629
Total Pre-School Grant			<u>96,922</u>	<u>96,922</u>
Total Special Education Cluster			<u>186,922</u>	<u>194,394</u>
Even Start	125690-EVS1-2005	84.213	3,298	6,411
	125690-EVS1-2006		155,236	146,869
Total - Even Start			<u>158,534</u>	<u>153,280</u>
Title I	125690-C1SD-2006	84.010	<u>21,705</u>	<u>21,705</u>
Total Department of Education			<u>367,161</u>	<u>369,379</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	248,859	248,859
State Childrens Health Insurance Program		93.767	18,214	18,214
Total Department of Health and Human Services			<u>267,073</u>	<u>267,073</u>
Total Federal Financial Assistance			<u>\$ 634,234</u>	<u>\$ 636,452</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, 2006**

NOTE A - SIGNIFICANT ACCOUNTING POLICIES

The accompanying Federal Awards Expenditures Schedule (the Schedule) summarizes activity of the ESC'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 ESC contribute non-Federal funds (matching funds) to support the Federally-funded programs. The ESC has complied with the matching requirements. The expenditure of non-Federal matching funds is not included on the Schedule.

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Mary Taylor, CPA

Auditor of State

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, Ohio (the ESC), as of and for the year ended June 30, 2006, which collectively comprise the ESC's basic financial statements and have issued our report thereon dated March 30, 2007. 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 ESC's internal control over financial reporting to determine our auditing procedures 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.

Compliance and Other Matters

As part of reasonably assuring whether the ESC'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

Erie-Huron-Ottawa Educational Service Center
Erie County
Independent Accountants' Report on Internal Control
Over Financial Reporting and on Compliance and
Other Matters Required by *Government Auditing Standards*
Page 2

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 "Mary Taylor". The signature is written in a cursive, flowing style.

Mary Taylor, CPA
Auditor of State

March 30, 2007



Mary Taylor, CPA

Auditor of State

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 ESC) 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, 2006. The summary of auditor's results section of the accompanying schedule of findings identifies the ESC's major federal program. The ESC'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 ESC'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 ESC'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 ESC'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 20, 2006.

Internal Control Over Compliance

The ESC'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 ESC'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.



Mary Taylor, CPA
Auditor of State

March 30, 2007

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

**SCHEDULE OF FINDINGS
OMB CIRCULAR A -133 § .505
JUNE 30, 2006**

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 XIX 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



Mary Taylor, CPA
Auditor of State

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 10, 2007