MADISON COMMUNITY SCHOOL
CUYAHOGA COUNTY

REGULAR AUDIT

FOR THE YEAR ENDED JUNE 30, 2007

Mary Taylor, CPA
Auditor of State

MADISON COMMUNITY SCHOOL
CUYAHOGA COUNTY

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Mary Taylor, CPA
Auditor of State

INDEPENDENT ACCOUNTANTS' REPORT

Madison Community School
Cuyahoga County
2015 West 95th Street
Cleveland, Ohio 44102

To the Board of Trustees:

We have audited the accompanying basic financial statements of Madison Community School, Cuyahoga County, Ohio, (the School) as of and for the year ended June 30, 2007, as listed in the table of contents. These financial statements are the responsibility of the School's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Comptroller General of the United States' *Government Auditing Standards*. Those standards require that we plan and perform the audit to reasonably assure whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Madison Community School, Cuyahoga County, Ohio, as of June 30, 2007, and the changes in financial position and its cash flows 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 February 7, 2008, on our consideration of the School's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. While we did not opine on the internal control over financial reporting or on compliance, that report describes the scope of our testing of internal control over financial reporting and compliance and the results of that testing. That report is an integral part of an audit performed in accordance with *Government Auditing Standards*. You should read it in conjunction with this report in assessing the results of our audit.

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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.

Mary Taylor

Mary Taylor, CPA
Auditor of State

February 7, 2008

The discussion and analysis of Madison Community School's (MDCS) financial performance provides an overall review of financial activities for the fiscal year ended June 30, 2007. The intent of this discussion and analysis is to look at the financial performance of MDCS as a whole. Readers should also review the Notes to the Financial Statements and the Financial Statements to enhance their understanding of the financial performance of MDCS.

Financial Highlights

Key financial highlights for 2007 include the following:

- In total, net assets increased $207,402, which represents a 107.7% increase from 2006. This increase is due primarily to increased enrollment, causing increased state and federal funding, and improved operating efficiencies in operating the school. MDCS also received private grants during the year.

- Total assets increased $155,821, which represents a 61.4% increase from 2006. This is due to an increase in cash of $96,483, a decrease in other current assets of $24,418 (collections of receivables) and an increase in net capital assets of $83,756. The cash balance increase is due primarily to the increased enrollment and improved operating efficiencies of the school.

- Liabilities decreased $51,581 which represents an 84.0% decrease from 2006. Current liabilities at fiscal year end include accounts payable of $8,292 and deferred revenue of $1,497.

- Operating revenues increased by $285,169, which represents a 34.1% increase from 2006. This increase is a direct result of increased enrollment causing a $281,769 increase in state funding. Other revenue also increased $3,400 primarily from the federal lunch program.

- Expenses increased by $450,691, which represents a 52.6% increase from 2006. Operating expense increases are due to personnel additions, increased student services, increased administrative costs and additional purchases of supplies and materials directly related to the growth of the school. Additionally, equipment and materials were purchased with non-operating revenues (mainly federal charter school start-up and lunch programs).

- Non-operating revenues increased by $211,224, which represents a 116.6% increase from 2006. This increase is due mostly to increased Federal and State Grants (primarily federal charter school start-up and lunch programs) in the amount of $200,646 as well as increases in interest earned of $1,241 and private contributions of $9,337.

Using this Financial Report

This report consists of three parts, Management's Discussion and Analysis, the Financial Statements and the Notes to the Financial Statements. The Financial Statements include a Statement of Net Assets, a Statement of Revenues, Expenses and Changes in Net Assets and a Statement of Cash Flows.

Statement of Net Assets

The Statement of Net Assets looks at how well MDCS has performed financially through June 30, 2007. This statement includes all of the assets, liabilities and net assets using the accrual basis of accounting, which is the accounting method used by most private-sector companies. This basis of accounting takes into account all revenues earned and expenses incurred during the year, regardless as to when the cash is received or expended.

The following schedule provides a summary Statement of Net Assets for fiscal years ended June 30, 2007 and 2006 for MDCS.

	2007	2006
Assets		
Cash	$ 259,703	$ 163,220
Other Current Assets	18,874	43,292
Security Deposits	6,000	6,000
Capital Assets	125,193	41,437
Total Assets	409,770	253,949
Liabilities		
Current Liabilities	9,789	61,370
Total Liabilities	9,789	61,370
Net Assets		
Investment in capital assets net of related debt	125,193	41,437
Unrestricted	274,788	151,142
Total Net Assets	$ 399,981	$ 192,579

Net Assets increased $207,402, due primarily to increased enrollment and improved operating efficiencies. For assets, cash increased $96,483; due from other governments decreased $24,478; accounts receivable increased $60, and net capital assets increased $83,756 from 2006. For liabilities, accounts payable decreased $33,942; due to other governments decreased $13,376; accrued wages and benefits decreased $3,100 and deferred revenues decreased $1,163 from 2006.

Statement of Revenues, Expenses and Changes in Net Assets

The Statement of Revenues, Expenses and Changes in Net Assets reports operating and non-operating activities for the fiscal year ended June 30, 2007.

The following schedule provides a summary of the Statement of Revenues, Expenses and Changes in Net Assets for MDCS for fiscal years ended June 30, 2007 and 2006.

	2007	2006
Revenues		
Foundation and Poverty Based Assistance Revenues	$1,096,029	$ 814,260
Other Operating Revenues	25,673	22,273
Operating Revenues	1,121,702	836,533
Interest	1,241	0
Federal and State Grants	376,691	176,045
Private Grants and Contributions	14,391	5,054
Non-Operating Revenues	392,323	181,099
Total Revenues	1,514,025	1,017,632
Expenses		
Salaries	481,680	323,928
Fringe Benefits	139,956	89,278
Purchased Services	420,024	287,985
Materials and Supplies	183,574	99,384
Capital Outlay	30,003	22,600
Depreciation	28,638	9,375
Other Operating Expenses	22,748	23,382
Total Expenses	1,306,623	855,932
Net Income	207,402	161,700
Net Assets at Beginning of Year	192,579	30,879
Net Assets at End of Year	$ 399,981	$ 192,579

Net Assets increased in both fiscal years ending June 30, 2006 and 2007. This is due to increased enrollment and improved operating efficiencies for both years. Although certain expenditures such as salaries will increase or decrease as the number of classes increase and decrease other costs remain fixed such as facilities costs resulting in more efficient operations. Additionally, grants have been received for capital improvements and to purchase various educational programs and equipment.

Overall, revenues increased by $496,393 from 2006 to 2007. The most significant item in revenues is Foundation and Poverty Based Assistance funds which increased $281,769 due to increasing enrollment and increases in the formula amount. Other revenues also increased because of the expanded school lunch program in 2007. Revenue increases of $200,646 occurred in Federal and State Grants due mainly to increased federal charter school start-up grants, title allocations and lunch program. Interest income and private contributions both increased from 2006.

In total, expenses increased from 2006 to 2007. Salaries and Fringe Benefits increased $208,430 due to additional staffing and annual increases. Purchased Services increased $132,039 due to an increased lunch program and additional pupil support services, administrative services and occupancy costs. Materials and Supplies increased $84,190 and Capital Outlay increased $7,403 due to purchasing text books, classroom supplies, furniture and equipment for classroom expansion. Depreciation increased $19,263 as a direct result of purchases of equipment and furniture during the year. Other Operating Expenses decreased $634 due to decreases in insurances.

Capital Assets

As of June 30, 2007, MDCS had $125,193 invested in computers and office equipment, furniture and equipment, and building improvements, net of depreciation. This is a $83,756 increase over June 30, 2006.

The following schedule provides a summary of Capital Assets as of June 30, 2007 and 2006 for MDCS.

	2007	**2006**
Capital Assets (net of depreciation)		
Building Improvements	$4,039	$8,078
Computers and Office Equipment	62,156	27,750
Furniture, Equipment & Materials	58,998	5,609
Net Capital Assets	$125,193	$41,437

For more information on capital assets see the Notes to the Financial Statements.

Current Financial Issues

Madison Community School opened in the fall of 2004. In its third year of operations it has grown from 35 students, three teaching staff members and expenses of $387,165 to a total of 154 students, 18 teaching staff members and expenses of $1,306,623. We are currently exploring bond financing to purchase and renovate the building that MDCS currently occupies so that we may further improve the position of the school for further growth. As MDCS' enrollment moves to capacity we will continue to maintain the high level of services we currently offer, to provide a strong educational product to our students and families and to maintain the reputation we have developed during these initial years.

Contacting the School's Financial Management

This financial report is designed to provide our constituents with a general overview of the finances for MDCS and to show accountability for the monies it receives. If you have any questions about this report or need additional information please contact Thomas F. Babb, CPA, Treasurer, by mail at Constellation Schools, 5983 West 54th Street, Parma, Ohio 44129; by e-mail at babb.thomas@constellationschools.com; by calling 440.845.7688; or by faxing 440.845.7689.

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Madison Community School
Cuyahoga County
Statement of Net Assets
As of June 30, 2007

Assets:	
Current Assets:	
Cash	$259,703
Due from Other Governments	18,814
Accounts Receivable	60
Total Current Assets	278,577
Non-Current Assets:	
Security Deposit	6,000
Capital Assets (Net of Accumulated Depreciation)	125,193
Total Non-Current Assets	131,193
Total Assets	409,770
Liabilities:	
Current Liabilities:	
Accounts Payable	8,292
Deferred Revenue	1,497
Total Current Liabilities	9,789
Net Assets:	
Investment in capital assets, net of related debt	125,193
Unrestricted	274,788
Total Net Assets	$399,981

The accompanying notes to the financial statements are an integral part of this statement.

Madison Community School
Cuyahoga County
Statement of Revenues, Expenses and
Changes in Net Assets
For the Fiscal Year Ended June 30, 2007

Operating Revenues:	
Foundation and Poverty Based Assistance Revenues	$1,096,029
Other Operating Revenues	25,673
Total Operating Revenues	1,121,702
Operating Expenses:	
Salaries	481,680
Fringe Benefits	139,956
Purchased Services	420,024
Materials and Supplies	183,574
Capital Outlay	30,003
Depreciation	28,638
Other Operating Expenses	22,748
Total Operating Expenses	1,306,623
Operating Loss	(184,921)
Non-Operating Revenues:	
Interest	1,241
Federal and State Grants	376,691
Private Grants and Contributions	14,391
Total Non-Operating Revenues	392,323
Net Income	207,402
Net Assets at Beginning of the Year	192,579
Net Assets at End of Year	$399,981

The accompanying notes to the financial statements are an integral part of this statement.

Madison Community School
Cuyahoga County
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2007

Increase (Decrease) in Cash:	
Cash Flows from Operating Activities:	
Cash Received from State of Ohio	$1,082,698
Cash Payments to Suppliers for Goods and Services	(829,962)
Cash Payments to Employees for Services	(484,780)
Other Operating Revenues	24,450
Net Cash Used for Operating Activities	(207,594)
Cash Flows from Noncapital Financing Activities:	
Federal and State Grants Received	400,839
Private Grants and Contributions Received	14,391
Net Cash Provided by Noncapital Financing Activities	415,230
Cash Flows from Capital and Related Financing Activities:	
Payments for Capital Acquisitions	(112,394)
Net Cash Used for Capital and Related Financing Activities	(112,394)
Cash Flows from Investing Activities:	
Interest	1,241
Net Cash Provided by Investing Activities	1,241
Net Increase in Cash	96,483
Cash at Beginning of Year	163,220
Cash at End of Year	$259,703

The accompanying notes to the financial statements are an integral part of this statement.

Madison Community School
Cuyahoga County
Statement of Cash Flows
For the Fiscal Year Ended June 30, 2007
(Continued)

Reconciliation of Operating Loss to Net Cash Used for Operating Activities

Operating Loss	($184,921)
Adjustments to Reconcile Operating Loss to Net Cash Used for Operating Activities:	
Depreciation	28,638
Changes in Assets and Liabilities:	
Decrease in Due from Other Governments	330
(Increase) in Accounts Receivable	(60)
(Decrease) in Accounts Payable	(33,942)
(Decrease) in Due Other Governments	(13,376)
(Decrease) in Accrued Wages and Benefits	(3,100)
(Decrease) in Deferred Revenue	(1,163)
Total Adjustments	(22,673)
Net Cash Used for Operating Activities	($207,594)

The accompanying notes to the financial statements are an integral part of this statement.

I. Description of the School and Reporting Entity

Madison Community School (MDCS) is a nonprofit corporation established on December 5, 2003 pursuant to Ohio Revised Code Chapters 3314 and 1702 to maintain and provide a school exclusively for any educational, literary, scientific and related teaching service that qualifies as an exempt organization under §501(c)(3) of the Internal Revenue Code. On March 28, 2006, MDCS received a determination letter confirming tax-exempt status with the Internal Revenue Service under section 501(c)(3) of the Internal Revenue Code. Management is not aware of any course of action or series of events that have occurred that might adversely affect MDCS' tax-exempt status. MDCS, which is part of Ohio's education program, is independent of any school district. MDCS may sue and be sued, acquire facilities as needed, and contract for any services necessary for the operation of MDCS.

On January 20, 2004 MDCS was approved for operations under a contract between the Governing Authority of MDCS and Lucas County Educational Service Center (LCESC) as their sponsor. The contract with LCESC was subsequently renewed effective November 2, 2006. Under the terms of the contract LCESC will provide sponsorship services for a fee. See Note XI for further discussion of the sponsor services. MDCS entered into an agreement with Constellation Schools (CS) to provide management services for the fiscal year. See Note XI for further discussion of this management agreement.

MDCS operates under a five-member Board of Directors. The Board is responsible for carrying out the provisions of the contract, which include, but are not limited to, state-mandated provisions regarding student population, curriculum, academic goals, performance standards, admission standards, and qualification of teachers. The Board of Directors controls MDCS' instructional facility staffed by sixteen certificated full time teaching personnel who provide services to 154 students.

Beginning on February 16, 2007, the board members for MDCS also serve as the board for Parma Community School. Previous to February 16, 2007 the board members of MDCS were also board members of Old Brooklyn Community School, Parma Community School, Elyria Community School, Lorain Community School, Westpark Community School, Mansfield Community School, Puritas Community School, Stockyard Community School, Lorain Academy for Gifted Students, Lorain Community Middle School, Old Brooklyn Community Middle School, Westpark Community Middle School, Outreach Academy for Children with Disabilities and Puritas Community Middle School.

On March 27, 2007 MDCS changed its legal name to Constellation Schools: Madison Community Elementary, but continues to operate as Madison Community School.

II. Summary of Significant Accounting Policies

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

1. Basis of Presentation

Enterprise accounting is used to account for operations that are financed and operated in a manner similar to private business enterprises where the intent is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or where it has been decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability or other purposes.

2. Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment is determined by its measurement focus. Enterprise accounting uses a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities are included on the Statement of Net Assets. Operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total assets.

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. MDCS prepares financial statements using the accrual basis of accounting. Revenues resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded when the exchange takes place. Revenues resulting from non-exchange transactions, in which MDCS receives value without directly giving equal value in return, such as grants and entitlements, are recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the fiscal year when the resources are required to be used or the fiscal year when the use is first permitted; matching requirements, in which MDCS must provide local resources to be used for a specified purpose; and expenditure requirements, in which resources are provided to MDCS on a reimbursement basis. Expenses are recognized at the time they are incurred.

3. Cash

All monies received by MDCS are deposited in demand deposit accounts.

4. Budgetary Process

Pursuant to Ohio Revised Code Chapter 5705.391 MDCS prepares and adopts an annual budget which includes estimated revenues and expenditures for the fiscal year and a five year forecast of revenues and expenditures. MDCS will from time to time adopt budget revisions as necessary.

5. Due From Other Governments and Accounts Receivable

Moneys due MDCS for the year ended June 30, 2007 are recorded as Due From Other Governments and as Accounts Receivable. A current asset for the receivable amount is recorded at the time of the event causing the moneys to be due.

6. Prepaid Employee Withholding

Payments made to vendors for voluntary employee benefits prior to collection from the employee that benefit future periods are recorded as prepaid employee withholding. A current asset for the prepaid amount is recorded at the time of the payment and is subsequently reduced upon collection by payroll withholding.

7. Capital Assets and Depreciation

Capital assets are capitalized at cost and updated for additions and retirements during the year. Donated capital assets are recorded at their fair market values as of the dates received. All items with a useful life of one year or greater and a value of $500 or more 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 capitalized.

All capital assets are depreciated. Depreciation of building improvements, computers, office equipment and furniture and equipment is computed using the straight-line method over their estimated useful lives. Improvements to capital assets are depreciated over the remaining useful lives of the related capital assets. Estimated useful lives are as follows:

Capital Asset Classification	**Years**
Building Improvements	5
Computers and Office Equipment	3
Furniture, Equipment and Materials	10

8. Intergovernmental Revenues

MDCS currently participates in the State Foundation Program and the State Poverty Based Assistance Program. Revenues received from these programs are recognized as operating revenues in the accounting period in which all eligibility requirements have been met.

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

MDCS also participates in the Federal Charter School Grant Program through the Ohio Department of Education. Under this program, MDCS was awarded $150,000 in fiscal year 2007 to offset start-up costs of the School. During fiscal year 2007, $150,000 from the award was received as well as $32,809 from a previous award. Revenue received from this program is recognized as non-operating revenue on the accompanying financial statements.

Amounts awarded under the above named programs for the 2007 school year totaled $1,472,720.

9. Private Grants and Contributions

MDCS received grants and contributions from private sources to support the schools programs. Private grants and contributions are recognized as non-operating revenues in the accounting period in which they are received. Amounts received for the 2007 school year totaled $14,391.

10. Compensated Absences

Vacation is taken in a manner which corresponds with the school calendar; therefore, MDCS does not accrue vacation time as a liability.

Sick leave benefits are earned at the rate of one and one-quarter day per month and can be accrued up to a maximum of one hundred twenty days. MDCS will accept the transfer of sick days from another school district up to the maximum accrual amount. No financial accrual for sick time is made since unused sick time is not paid to employees upon employment termination.

11. Use of Estimates

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

12. Deferred Revenue

Deferred revenue arises when assets are recognized before revenue recognition criteria have been satisfied. The deferred revenue for MDCS consists of materials fees received in the current year which pertains to the next school year.

III. Deposits

At fiscal year end June 30, 2007, the carrying amount of MDCS' deposits totaled $259,703 and its bank balance was $324,808. Based on the criteria described in GASB Statement No. 40, "Deposit and Investment Risk Disclosure," as of June 30, 2007, $224,808 of the bank balance was exposed to custodial risk as discussed below, while $100,000 was covered by the Federal Depository Insurance Corporation.

Custodial credit risk is the risk that in the event of bank failure, MDCS will not be able to recover the deposits. All deposits are collateralized with eligible securities in amounts equal to at least 105% of the carrying value of the deposits. Such collateral, as permitted by the Ohio Revised Code, is held in single financial institution collateral pools at the Federal Reserve Banks or at member banks of the federal reserve system, in the name of the respective depository bank and pledged as a pool of collateral against all of the public deposits it holds or as specific collateral held at the Federal Reserve Bank in the name of MDCS.

IV. Capital Assets

A summary of capital assets at June 30, 2007 follows:

	Balance 6/30/06	Additions	Deletions	Balance 6/30/07
Capital Assets Being Depreciated:				
Building Improvements	$15,160	0	0	15,160
Computers/Office Equipment	36,421	56,949	0	93,370
Furniture, Equipment & Materials	6,437	55,445	0	61,882
Total Capital Assets Being Depreciated:	58,018	112,394	0	170,412
Less Accumulated Depreciation:				
Building Improvements	(7,082)	(4,039)	0	(11,121)
Computers/Office Equipment	(8,671)	(22,543)	0	(31,214)
Furniture and Equipment	(828)	(2,056)	0	(2,884)
Total Accumulated Depreciation:	(16,581)	(28,638)	0	(45,219)
Total Capital Assets, Net of Accumulated Depreciation	$41,437	$83,756	$0	$125,193

V. Purchased Services

Purchased Services include the following:

Instruction	$57,503
Pupil Support Services	55,854
Staff Development & Support	10,047
Administrative	164,381
Occupancy Costs	88,018
Food Services	44,221
Total	$420,024

VI. Operating Lease

MDCS leases its facilities at 2015 West 95th Street, Cleveland from Madison Avenue Baptist Church under a forty-seven month lease agreement effective August 1, 2004 and expiring June 30, 2008. Monthly payments under the terms of the lease are $6,000. The lease also provides that MDCS will pay $6,000 for a security deposit at the time the lease was signed. In addition, MDCS pays Madison Avenue Baptist Church $500 for cleaning services. MDCS has an option to purchase the building at a price of $800,000. During fiscal year 2006 rents totaled $72,000.

VII. Risk Management

1. Property and Liability Insurance

MDCS 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. For fiscal year 2007, MDCS contracted with Cincinnati Insurance Company for all of its' insurance.

General liability is covered at $4,000,000 single occurrence limit and $5,000,000 aggregated. Hired and Non-Owned Vehicles are covered at $500,000 combined single limit of liability. Other coverage includes Employee Crime, School Leaders Errors & Omissions, Sexual Abuse and Misconduct, Electronic Data Processing and Business Interruption.

2. Workers' Compensation

MDCS makes premium payments to the Ohio Worker's Compensation System for employee injury coverage. There has been one claim filed by MDCS employees with the Ohio Worker's Compensation System between January 1, 2000 and June 30, 2007. The total payments made for this claim have been $553. In the opinion of management, these claims will not have a material adverse effect on the overall financial position of MDCS as June 30, 2007.

3. Employee Medical, Dental, and Life Benefits

MDCS provides medical, dental and life insurance benefits to all full time employees. Employees participate in premium payments through pretax payroll deductions. Total insurance benefits paid by MDCS for the fiscal year is $58,221.

VIII. Defined Benefit Pension Plans

1. School Employees Retirement System

MDCS contributes to the School Employees Retirement System of Ohio (SERS), a cost-sharing multiple-employer defined benefit pension plan. SERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by state statute per 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 St., Suite 100, Columbus, Ohio 43215-3746.

Plan members are required to contribute 10 percent of their annual covered salary and MDCS is required to contribute at an actuarially determined rate. The current rate for MDCS is 14 percent of annual covered payroll. A portion of MDCS' contribution is used to fund pension obligations with the remainder being used to fund health care benefits; for fiscal year 2007 (the latest information available), 10.68 percent of annual covered salary was the portion to fund pension obligations. The contribution requirements of plan members and employers are established and may be amended, up to a statutory maximum amount, by the SERS' Retirement Board. MDCS' required contribution for pension obligations to SERS for the fiscal years ended June 30, 2007, 2006 and 2005 were $3,921, $2,326 and $1,471. For fiscal year 2007, all required contributions have been made.

2. State Teachers Retirement System

MDCS 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 East Broad Street, Columbus, Ohio 43215-3771, by calling (614)227-4090, or by visiting the STRS Ohio web site at www.strsoh.org.

New members have a choice of three retirement plans, a Defined Benefit (DB) Plan, a Defined Contribution (DC) Plan and a Combined Plan. The DB plan offers an annual retirement allowance based on final average salary times a percentage that varies based on years of service, or an allowance based on member contributions and earned interest matched by STRS Ohio funds divided by 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 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 the 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 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, 2007, plan members were required to contribute 10 percent of their annual covered salary. MDCS was required to contribute 14 percent. For fiscal year 2007 the portion used to fund pension obligations was 13 percent. Contribution rates are established by the State Teachers Retirement Board, upon recommendations 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.

MDCS' required contribution for pension obligations to STRS Ohio for the fiscal years ended June 30, 2007, 2006 and 2005 were $57,845, $39,252 and $14,048. For fiscal year 2007, all required contributions have been made.

IX. Post-Employment Benefits

MDCS 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 on a pay-as-you-go basis.

All 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 the 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, 2007, the STRS Ohio Board allocated employer contributions equal to one percent of covered payroll to the Health Care Stabilization Fund. For MDCS, this amount equaled $4,450 during fiscal 2007.

STRS Ohio pays health care benefits from the Health Care Stabilization Fund. At June 30, 2006, (the latest information available) the balance in the Fund was $3.5 billion. For the year ended June 30, 2006, net health care costs paid by STRS were $282,743,000 and STRS had 119,184 eligible benefit recipients.

For SERS, coverage is made available to service retirees with ten or more years of qualifying service credit, and to disability and survivor benefit recipients. All retirees and beneficiaries are required to pay a portion of their premiums for health care. The portion is based on years of service, Medicare eligibility and retirement status.

After the allocation for the 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, 2007, employer contributions to fund health care benefits were 3.32 percent of covered payroll, compared to 3.42 percent of covered payroll in fiscal year 2006. 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 2007, the minimum pay was established at $35,800. However, the surcharge is capped at 2 percent of each employer’s SERS salaries. For MDCS, the amount contributed to fund health care benefits, including surcharge, during the 2007 fiscal year equaled $1,774.

The surcharge added to the unallocated portion of the 14 percent employer contribution rate, provides for maintenance of the asset target level of the health care fund. The target level of the health care reserve is 150 percent of the projected claims less premium contributions for the next fiscal year. Expenses for health care for the fiscal year ended June 30, 2006 (the latest information available), were $158,751,207. At June 30, 2006, SERS had net assets available for health care benefits of $295.6 million. SERS has 59,492 participants eligible to receive health care benefits.

X. Contingencies

1. Grants

MDCS received financial assistance from Federal and State agencies in the form of grants. The disbursement of funds received under these programs 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 MDCS. However, in the opinion of management, any such disallowed claims will not have a material adverse effect on the overall financial position of MDCS at June 30, 2007.

2. Litigation

A lawsuit entitled *Beverly Blount-Hill et al. v. State of Ohio, et al., Case #: 3:04CV197* was filed in the US District Court, Southern District of Ohio, Western Division in October 2004. The suit alleges that the funding provisions of the Ohio Community Schools Act, O.R.C. Section 3314 violate both the Ohio and Federal constitutions. If the funding scheme is determined to be unconstitutional, it could have financial ramifications for all community/charter schools. The case is currently pending, and the effect of this suit, if any, on MDCS cannot be presently determined.

3. Enrollment FTE

The Ohio Department of Education conducts reviews of enrollment and full-time equivalency (FTE) calculations made by the schools. These reviews are conducted to ensure the schools are reporting accurate student enrollment data to the State, upon which state foundation funding is calculated. The conclusions of this review could result in state funding being adjusted. As of the date of this report adjustments to the state funding received during fiscal year 2007 are reflected in the financial statements.

XI. Sponsorship and Management Agreements

MDCS entered into an agreement with Lucas County Educational Service Center (LCESC) to provide sponsorship and oversight services as required by law. The agreement is effective October 16, 2003. Sponsorship fees are calculated as a percentage of state funds received by MDCS, from the State of Ohio. During the 2007 fiscal year the fee changed from 1% to 1.5%. The total amount due from MDCS for fiscal year 2007 was $15,159 of which $1,559 was outstanding as of June 30, 2007.

MDCS entered into an agreement with Constellation Schools (CS) to provide legal, financial, and business management services for fiscal year 2007. The agreement was for a period of one year, effective July 1, 2006. Management fees are calculated as 11.5% of the Fiscal Year 2007 Foundation payment received by MDCS, as reported in the Monthly Community School Foundation Report. The total amount due from MDCS for the fiscal year ending June 30, 2007 was $126,043 all of which was paid prior to June 30, 2007.

In addition, MDCS is participating in a payroll bonus reserve established through CS. Payroll bonus reserve fees are calculated as 1% of the Fiscal Year 2007 Foundation payment received by MDCS, as reported in the Monthly Community School Foundation Report. The total amount due from MDCS for the fiscal year ending June 30, 2007 was $10,960 all of which was paid prior to June 30, 2007.

XII. Subsequent Events – Bond Financing

On January 23, 2008 the owner of the building MDCS occupies under a lease agreement sold the building to The Industrial Development Authority of the County of Pima (IDA). As part of a financing arrangement MDCS will lease the property from IDA who issued bonds for the purchase and renovation of the existing structure.

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*

Madison Community School
Cuyahoga County
2015 West 95th Street
Cleveland, Ohio 44102

To the Board of Trustees:

We have audited the financial statements of the Madison Community School, Cuyahoga County, Ohio, (the School) as of and for the year ended June 30, 2007, and have issued our report thereon dated February 7, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in the Comptroller General of the United States' *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the School's internal control over financial reporting as a basis for designing our audit procedures for expressing our opinions on the financial statements, but not to opine on the effectiveness of the School's internal control over financial reporting. Accordingly, we have not opined on the effectiveness of the School's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the School's ability to initiate, authorize, record, process, or report financial data reliably in accordance with its applicable accounting basis, such that there is more than a remote likelihood that the School's internal control will not prevent or detect a more than inconsequential financial statement misstatement.

A material weakness is a significant deficiency, or combination of significant deficiencies resulting in more than a remote likelihood that the School's internal control will not prevent or detect a material financial statement misstatement.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all internal control deficiencies that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider material weaknesses, as defined above.

We noted certain matters that we reported to the School's management in a separate letter dated February 7, 2008.

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Compliance and Other Matters

As part of reasonably assuring whether the School's financial statements are free of material misstatement, we tested its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could directly and materially affect the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and accordingly, we do not express an opinion. The results of our tests disclosed no instances of noncompliance or other matters we must report under *Government Auditing Standards*.

We intend this report solely for the information and use of the audit committee, management, the Board of Trustees and the School's Sponsor. We intend it for no one other than these specified parties.

Mary Taylor

Mary Taylor, CPA
Auditor of State

February 7, 2008

Mary Taylor, CPA
Auditor of State

MADISON COMMUNITY SCHOOL

CUYAHOGA 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
MARCH 11, 2008

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