



**Auditor of State
Betty Montgomery**

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

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**Auditor of State
Betty Montgomery**

INDEPENDENT ACCOUNTANTS' REPORT

Toledo School for the Arts
Lucas County
425 Jefferson Avenue
Toledo, Ohio 43604-1060

To the Governing Board:

We have audited the Balance Sheet of the Toledo School for the Arts, Lucas County, (the School) as of and for the year ended June 30, 2003, and the related Statement of Revenues, Expenses, and Changes in Accumulated Deficit, and the Statement of Cash Flows for the year ended June 30, 2003. 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 *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about 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 that 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 School as of June 30, 2003, and the results of its operations and cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming the School will continue as a going concern. As shown in the financial statements, the School has incurred an operating loss in the amount of \$174,125 for the year ended June 30, 2003, has a working capital deficiency of \$421,416 as of June 30, 2003, an accumulated deficit of \$313,394, and has been unable to pay its obligations when due. Accordingly, there is substantial doubt about the School's ability to continue as a going concern. Management's plans in regards to these matters are discussed in Note 18. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 2, 2004, 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 grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.



Betty Montgomery
Auditor of State

April 2, 2004

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

**BALANCE SHEET
AS OF JUNE 30, 2003**

Assets

Current Assets

Cash	\$ 22,366
Intergovernmental Receivable	15,032
Prepaid Items	4,569
Total Current Assets	<u>41,967</u>

Non-Current Assets

Security Deposit	13,903
Fixed Assets (Net of Accumulated Depreciation)	189,119
Total Assets	<u><u>\$ 244,989</u></u>

Liabilities and Fund Equity

Current Liabilities

Accounts Payable	\$ 43,349
Accrued Wages Payable	141,587
Intergovernmental Payable	29,897
Due to Students	2,895
Accrued Interest Payable	547
Notes Payable	238,312
Capital Leases Payable	6,796
Total Current Liabilities	<u>463,383</u>

Long-Term Liabilities

Capital Leases Payable	7,076
Total Liabilities	<u>470,459</u>

Fund Equity

Contributed Capital	87,924
Accumulated Deficit	(313,394)
Total Fund Equity	<u>(225,470)</u>
Total Liabilities and Fund Equity	<u><u>\$ 244,989</u></u>

THE NOTES TO THE FINANCIAL STATEMENTS ARE AN INTEGRAL PART OF THIS STATEMENT.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

**STATEMENT OF REVENUES, EXPENSES, AND
CHANGES IN ACCUMULATED DEFICIT
FOR THE YEAR ENDED JUNE 30, 2003**

Operating Revenues

Foundation Payments	\$ 1,397,054
Disadvantaged Pupil Impact Aid	19,180
Career Tech Adult Education	91,878
Food Services	3,542
Classroom Materials and Fees	36,527
Other Operating Revenues	46,306
Total Operating Revenues	1,594,487

Operating Expenses

Salaries	1,004,288
Fringe Benefits	243,670
Purchased Services	246,605
Materials and Supplies	83,019
Depreciation	120,240
Other Operating Expenses	70,790
Total Operating Expenses	1,768,612
Operating Loss	(174,125)

Non-Operating Revenues (Expenses)

Grants - Federal	77,816
Grants - State	7,990
Grants - Other	10,500
Interest Earnings	645
Contributions and Donations	36,069
Interest Charges	(15,456)
Total Non-Operating Revenues	117,564
Net Loss	(56,561)
Accumulated Deficit at Beginning of Year	(256,833)
Accumulated Deficit at End of Year	\$ (313,394)

THE NOTES TO THE FINANCIAL STATEMENTS ARE AN INTEGRAL PART OF THIS STATEMENT.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

**STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2003**

Increase (Decrease) in Cash and Cash Equivalents

Cash Flows from Operating Activities

Cash Received from State of Ohio	\$ 1,461,142
Cash Received from Food Services	3,542
Cash Received from Classroom Materials and Fees	36,527
Cash Received from Other Operating Revenue	49,435
Cash Payments to Suppliers for Goods and Services	(379,072)
Cash Payments to Employees for Services	(963,453)
Cash Payments for Employee Benefits	(234,828)
Cash Payments for Other Operating Uses	<u>(81,785)</u>
Net Cash Used for Operating Activities	<u>(108,492)</u>

Cash Flows from Noncapital Financing Activities

Grants - Federal	95,263
Grants - State	7,990
Grants - Other	10,500
Contributions and Donations	<u>36,069</u>
Net Cash Provided by Noncapital Financing Activities	<u>149,822</u>

Cash Flows from Capital and Related Financing Activities

Payments for Capital Acquisitions	(5,149)
Principal Payments	(16,608)
Interest Payments	<u>(16,338)</u>
Net Cash Used for Capital and Related Financing Activities	<u>(38,095)</u>

Cash Flows from Investing Activities

Interest on Investments	<u>645</u>
Net Cash Provided by Investing Activities	<u>645</u>

Net Increase in Cash and Cash Equivalents	3,880
Cash and Cash Equivalents at the Beginning of the Year	<u>18,486</u>
Cash and Cash Equivalents at the End of the Year	<u><u>\$ 22,366</u></u>

(Continued)

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

**STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2003
(Continued)**

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

Operating Loss	\$ (174,125)
Adjustments to Reconcile Operating Loss to Net Cash Used for Operating Activities	
Depreciation	120,240
Changes in Liabilities:	
(Increase)/Decrease in Accounts Receivable	7,269
(Increase)/Decrease in Intergovernmental Receivable	(11,824)
(Increase)/Decrease in Prepaid Items	(3,931)
Increase/(Decrease) in Accounts Payable	(41,860)
Increase/(Decrease) in Accrued Wages Payable	44,104
Increase/(Decrease) in Due to Students	903
Increase/(Decrease) in Intergovernmental Payable	<u>(49,268)</u>
Total Adjustments	<u>65,633</u>
Net Cash Used for Operating Activities	<u><u>\$ (108,492)</u></u>

THE NOTES TO THE FINANCIAL STATEMENTS ARE AN INTEGRAL PART OF THIS STATEMENT.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

**NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003**

1. DESCRIPTION OF THE SCHOOL AND REPORTING ENTITY

Toledo School for the Arts (the School) is a nonprofit corporation established pursuant to Ohio Revised Code Chapters 3314 and 1702. The School is an approved tax-exempt organization 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 the School's tax-exempt status. The School's objective is to provide students the opportunity to achieve personal and academic success through arts-based learning. The School's programs are currently available to students in grades 7 - 12. The School, which is part of the State's education program, is independent of any school district and is nonsectarian in its programs, admission policies, employment practices, and all other operations. The School may acquire facilities as needed and contract for any services necessary for the operation of the school.

The School was approved for operation under a contract with the Toledo City School District (the Sponsor) for a period of five years commencing June 22, 1998, with operations starting in July of 1999. This contract expired June 30, 2003. The School entered into a continuing contract with the Sponsor for a period of five years commencing July 1, 2003. The Sponsor is responsible for evaluating the performance of the School and has the authority to deny renewal of the contract at its expiration or terminate the contract prior to its expiration. The School entered into a separate agreement for the Treasurer of the Lucas County Educational Service Center to serve as the Chief Financial Officer of the School (see Note 13).

The School operates under the direction of a twenty member Governing Board. The Governing 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 qualifications of teachers. The Governing Board controls the School's one instructional/support facility staffed by 6 non-certified and 37 certificated full time teaching personnel who provide services to 274 students.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the School 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. The School 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 the School's accounting policies are described below.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

A. 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.

B. 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 balance sheet. Equity (i.e., net total assets) is segregated into contributed capital and accumulated deficit components. Operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total assets.

Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made.

The accrual basis of accounting is used for reporting purposes. Revenues are recognized when they are earned, and expenses are recognized when they are incurred.

C. Budgetary Process

Unlike other public schools located in the state of Ohio, community schools are not required to follow budgetary provisions set forth in Ohio Revised Code Chapter 5705, unless specifically provided in the School's contract with its Sponsor. The contract between the School and its Sponsor does prescribe an annual budget requirement in addition to preparing a 5-year forecast which is to be updated on an annual basis. The School follows a budget that is adopted and revised as needed.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2003

(Continued)

D. Cash and Cash Equivalents

All monies received by the School are accounted for by the School's fiscal agent, the Lucas County Educational Service Center. All cash received by the fiscal agent is maintained in separate bank accounts in the School's name. Monies for the School are maintained in these accounts or temporarily used to purchase short-term investments.

For purposes of the statement of cash flows and for presentation on the balance sheet, investments with original maturities of three months or less at the time they are purchased by the School are considered to be cash equivalents.

E. Fixed Assets and Depreciation

Fixed assets are capitalized at cost and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market value as of the dates received. The School does not possess any infrastructure.

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

Depreciation of furniture, equipment and leasehold improvements is computed using the straight-line method over an estimated useful life of five years. Improvements to fixed assets are depreciated over the remaining useful lives of the related fixed assets.

F. Intergovernmental Revenues

The School currently participates in the State Foundation Program, the State Disadvantaged Pupil Impact Aid (DPIA) Program, and the Career Tech Adult Education Program (CTA). Revenues received from these programs are recognized as operating revenues in the accounting period in which all eligibility requirements have been met.

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

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

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

Amounts awarded under the above named programs for the year ended June 30, 2003 totaled \$1,593,918.

G. Prepaid Items

Payments made to vendors for services that will benefit periods beyond June 30, 2003, are recorded as prepaid items using the consumption method by recording a current asset for the prepaid amount and reflecting the expense in the year in which services are consumed.

H. Estimates

The preparation of financial statements in conformity with generally accepted accounting principles accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

I. Contributed Capital

Contributed capital represents equity obtained from private sources provided to the School that are not subject to repayment. These assets are recorded at their fair market value on the date contributed. Depreciation on those assets acquired with contributed resources is expensed. There were no additions to contributed capital in the year ended 2003.

J. Compensated Absences

Vacation benefits are accrued as a liability as the benefits are earned if the employees' rights to receive compensation are attributable to services already rendered and it is probable that the School will compensate the employees for the benefits through paid time off or some other means. The School records a liability for accumulated vacation time when earned for all employees. There was no accrued vacation for the year ended 2003.

K. Security Deposit

The School entered into a lease for the use of a building for the operation of the School. Based on the lease agreement, a security deposit was required to be paid at the signing of the agreement. This amount is held by the lessor.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

3. ACCOUNTABILITY AND COMPLIANCE

The school is analyzing operations and admissions procedures to determine appropriate steps to alleviate the deficit (See Note 18).

4. DEPOSITS AND INVESTMENTS

At June 30, 2003, the carrying amount of the School's deposits was \$22,366 and the bank balance was \$51,398. The bank balance was covered by federal depository insurance.

5. RECEIVABLES

Receivables at June 30, 2003, consisted of intergovernmental (e.g., grants) receivables. All intergovernmental receivables are considered collectible in full due to the current year guarantee of federal funds.

6. FIXED ASSETS

A summary of the School's fixed assets at June 30, 2003, follows:

Leasehold Improvements	\$	380,370
Furniture and Equipment		220,826
Sub Total		601,196
Less Accumulated Depreciation		(412,077)
Net Fixed Assets	\$	189,119

7. RISK MANAGEMENT

A. Property and Liability

The School is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. For the fiscal year ended June 30, 2003, the School had the following insurance coverage:

General Liability per Occurrence	\$ 2,000,000
General Liability Aggregate	2,000,000
Commercial Liability	2,000,000
Personal/Advertising Injury Limit	1,000,000

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

General Liability per Occurrence – Umbrella	1,000,000
General Liability Aggregate – Umbrella	1,000,000
Commercial Liability – Umbrella	1,000,000
EDP Hardware (\$250 Deductible)	45,000
EDP Software (\$250 Deductible)	4,500
EDP Hardware & Software (\$250 Deductible)	10,000
Miscellaneous Scheduled Property (\$250 Deductible)	2,200
Commercial Automobile Coverage	1,000,000
Employee Dishonesty – Blanket (\$500 Deductible)	10,000
Forgery & Alteration (\$500 Deductible)	10,000
Employee Benefits Liability (\$1,000 Deductible)	1,000,000
Stop Gap Liability	1,000,000
Director’s and Officer’s Liability (\$2,500 Deductible)	1,000,000

Settled claims have not exceeded this commercial coverage in the past three years. The School owns no real estate, but leases a facility located at 425 Jefferson Avenue, Toledo, Ohio. (See Note 17)

B. Workers’ Compensation

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

8. DEFINED BENEFIT PENSION PLANS

A. School Employees Retirement System

The School contributes to the School Employees Retirement System of Ohio (SERS), a cost-sharing multiple employer defined benefit pension plan, administered by the School Employees Retirement Board. 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 financial report that includes financial statements and required supplementary information. The report may be obtained by writing to the School Employees Retirement System, 300 East Broad Street, Suite 100, Columbus, Ohio 43215-3746.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

For the fiscal year ended June 30, 2003, plan members were required to contribute 9 percent of their annual covered salary and the School was required to contribute an actuarially determined rate. The rate for fiscal year 2003 was 14 percent of annual covered payroll; 8.17 percent was the portion used to fund pension obligations. The contribution requirements of plan members and employers are established and may be amended, up to statutory maximum amounts by the SERS' Retirement Board. The School's required contribution for pension obligations to SERS for the year ended June 30, 2003, 2002, and 2001 were \$6,110, \$2,712 and \$3,545, respectively; 98.40 percent has been paid for the year ended 2003 and 100 percent has been paid for 2002 and 2001.

B. State Teachers Retirement System

The School contributes to the State Teachers Retirement System of Ohio (STRS), a cost-sharing, multiple-employer public employee retirement system administered by the State Teachers Retirement Board. STRS provides retirement and disability benefits to members and death and survivor benefits to beneficiaries. Benefits are established by Chapter 3307 of the Ohio Revised Code. STRS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to the State Teachers Retirement System, 275 East Broad Street, Columbus, Ohio 43215-3771.

New members have a choice of three retirement plans, a Defined Benefit Plan (DBP), a Defined Contribution Plan (DCP), and a Combined Plan (CP). The DBP offers an annual retirement allowance based on final average salary multiplied by a percentage that varies based on years of service or on an allowance based on member contributions and earned interest matched by STRS funds multiplied by an actuarially determined annuity factor. The DCP allows members to place all of 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 fifty and termination of employment. The CP offers features of both the DBP and DCP. In the CP, 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 DBP. DCP and CP members will transfer to the DBP during their fifth year of membership unless they permanently select the DCP or CP. 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 balance from the existing DBP into the DCP or CP. This option expired on December 31, 2001.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS

JUNE 30, 2003

(Continued)

A DBP or CP member with five or more years of 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 DCP 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, 2003, plan members were required to contribute 9.3 percent of their annual covered salary and the School is required to contribute 14 percent; 13 percent was the portion used to fund pension obligations. Contribution rates are established by STRS, upon recommendation of its consulting actuary, not to exceed statutory maximum rates of 10 percent for members and 14 percent for employers.

The School's required contributions for pension obligations for the DBP for the fiscal years ended June 30, 2003, 2002 and 2001 was \$112,632, \$58,718, and \$50,944, respectively; 98.06 percent being paid in 2003 and 100 percent has been contributed for the years ended 2002 and 2001. The unpaid contribution for the year ended 2003, in the amount of \$2,241, is recorded as a liability. Contributions for the DCP and CP for the fiscal year ended June 30, 2003, were \$2,895 made by the School District and \$2,958 made by plan members.

9. POSTEMPLOYMENT BENEFITS

The School provides comprehensive health care benefits to retired teachers and their dependents through the State Teachers Retirement System (STRS), and to retired non-certificated 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 obligation 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.

For STRS, all benefit recipients are required to pay a portion of health care costs in the form of a monthly premium. By Ohio Law, the cost of coverage paid from STRS funds shall be included in the employer contribution rate, currently 14 percent of covered payroll. The Governing Board allocated employer contributions equal to one percent of covered payroll to the Health Care Stabilization Fund for which payments for health care benefits are paid. For the School, this amount equaled \$8,887 for the year ended June 30, 2003. The balance in the Fund was \$3.011 billion at June 30, 2002 (the latest information available). For the fiscal year

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

ended June 30, 2002, net health care costs paid by STRS were \$354,697,000 and STRS had 105,300 eligible benefit recipients.

For SERS, coverage is made available to service retirees with ten or more years of qualifying service credit, disability and survivor benefit recipients. Members retiring on or after August 1, 1989, with less than twenty-five years of service credit must pay a portion of their premium for health care. The portion is based on years of service up to a maximum of 75 percent of the premium.

For the fiscal year ended June 30, 2003, employer contributions to fund health care benefits were 5.83 percent of covered payroll. 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 2003, the minimum pay had been established at \$14,500. For The School, the amount to fund health care benefits, including surcharge, was \$6,176 for fiscal year 2003.

The surcharge, added to the unallocated portion of the 14 percent employer contribution rate, provides for maintenance for 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 at June 30, 2002 (the latest information available), were \$182,946,777 and the target level was \$274.4 million. At June 30, 2002, SERS had net assets available for payment of health care benefits as \$335.2 million. SERS had approximately 50,000 participants currently receiving health care benefits.

10. OTHER EMPLOYEE BENEFITS

A. Compensated Absences

The criteria for determining vacation are derived from policies and procedures approved by the Governing Board.

B. Employee Medical, Dental and Vision Benefits

The School has contracted through Lucas County Educational Service Center to provide employee medical, dental, and vision insurance to its full-time employees who work 20 or more hours per week. The School pays the full amount of the monthly premiums for all selected coverage (medical, dental and/or vision). Employees electing the family coverage pay the difference in the premium.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

11. STATE SCHOOL FUNDING DECISION

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

The Supreme Court relinquished jurisdiction over the case and directed "...the Ohio General Assembly to enact a school-funding scheme that is thorough and efficient...."

The School is currently unable to determine what effect, if any, this decision will have on its future State funding and its financial operations.

12. CONTINGENCIES

A. Grants

The School received financial assistance from federal and state agencies in the form of grants. The disbursement of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and are subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the funds. However, in the opinion of management, any such disallowed claims will not have a material adverse effect on the overall financial position of the School at June 30, 2003.

B. Pending Litigation

A suit was filed in Franklin County Common Pleas Court on May 14, 2001, alleging that Ohio's Community (i.e., Charter) Schools program violates the state Constitution and state laws. On April 21, 2003 the court dismissed the counts containing constitutional claims and stayed the other counts pending appeal of the constitutional issues. The plaintiffs appealed to the Court of Appeals, the issues have been briefed, and the case was heard for oral argument on November 18th, 2003.

The effect of this suit, if any, on Toledo School for the Arts is not presently determinable.

C. State Funding

The Ohio Department of Education conducts reviews of enrollment data and full time equivalency (FTE) calculations made by the schools. These reviews are conducted to

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

ensure the schools are reporting accurate student enrollment data to the State, upon which state foundation funding is calculated. The adjustment as a result of the review was not material.

13. FISCAL AGENT

The school entered into a service agreement with the Treasurer of the Lucas County Educational Service Center to serve as the Chief Fiscal Officer of the School. As part of this agreement, the School shall compensate the Lucas County Educational Service Center two percent (2%) of the per pupil allotments paid to the School from the State of Ohio. The total contract payment of \$28,839 was paid during the year in full.

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

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

14. PURCHASED SERVICE EXPENSES

For the year ended June 30, 2003, purchased service expenses were payments for services rendered by various vendors, as follows:

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

PURCHASED SERVICES	
Professional and Technical Services	\$ 27,367
Property Services	183,849
Travel Mileage/Meeting Expenses	3,044
Communications	15,293
Contracted Craft or Trade Services	9,592
Transportation Services	6,843
Other Purchased Services	617
Total Purchased Services	\$ 246,605

15. DEBT

Debt outstanding for the School as of June 30, 2003 was as follows:

	Outstanding 06/30/02	Additions	Payments	Outstanding 06/30/03
General Note #1 (Sky Bank)	\$ 198,487	\$ -	\$ -	\$ 198,487
General Note #2 (Sky Bank)	29,866	-	41	29,825
Board Loan	20,000	-	10,000	10,000
	\$ 248,353	\$ -	\$ 10,041	\$ 238,312

The General Note #1 from Sky Bank is a line of credit issued on August 13, 1999, with an amount up to \$200,000. The terms of the note had a maturity date of April 30, 2002. The note was extended for another year and is now payable on October 30, 2003. The interest rate on this line of credit is variable, based on one percent over the prime rate. Total interest expense for the year ended June 30, 2003 was \$11,022 and was paid in full at year end.

The General Note #2 from Sky Bank is a promissory note issued on February 26, 2002, in the amount of \$30,000. The terms of the note had a maturity date of August 26, 2003. The note was extended for another six months and is now payable on February 26, 2004. The interest on this promissory note is 5.75 percent. Total interest expense for the year ended June 30, 2003 was \$1,687 and was paid in full at year end.

The board loan consisted of a \$10,000 loan issued from a board member of the School, on December 9, 2001 to cover rent expenses for the 2002 school year. The interest paid on this promissory note was \$994, of which \$547 was accrued at year end.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

16. CAPITALIZED LEASES

The School entered into a capitalized lease for the acquisition of copier equipment. The lease meets the criteria of a capital lease as defined by Statement of Financial Accounting Standards No. 13 "Accounting for Leases," which defines a capital lease generally as one which transfers benefits and risks of ownership to the lessee. The capital leases have been recorded as fixed assets at the present value of the minimum lease payments as the of the inception date.

The following is a schedule of the future minimum lease payments required under the capital leases and the present value of the minimum lease payments as of June 30, 2003. Payments for principal and interest totaled \$7,163 for the year ending June 30, 2003.

Year Ending June 30,	Equipment
2004	\$ 7,163
2005	6,612
2006	598
Total minimum lease payments	14,373
Less: amount representing interest	(501)
Present value of minimum lease payments	\$ 13,872

17. OPERATING LEASES

The School entered into an operating lease for the period August 1, 1999 through July 31, 2003 with Hillenbrand/Zaleski Secor, LLC to lease the third floor of its building for operation of the school facility. In addition, the lease was amended to include a one-year lease of the second floor through July 31, 2003. Lease payments totaled \$200,000 for the year. At year end, all rent owed to the lessor was paid in full.

In July of 2003, the School renewed the lease with Hillenbrand/Zaleski Secor, LLC for a one year term commencing on July 1, 2003. Rent payments of \$19,166 will be paid monthly to the lessor.

The following is a schedule of the future minimum payments required under the operating lease as of June 30, 2003.

Year Ending June 30,	
2004	\$ 230,000

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 2003
(Continued)

18. MANAGEMENT'S PLANS REGARDING ACCUMULATED DEFICIT (SEE NOTE 3)

The School has an accumulated deficit of \$313,394 for the year ended June 30, 2003, an operating loss of \$174,125, and had negative working capital of \$421,416. The School is analyzing operations and admissions procedures to determine appropriate steps to alleviate the deficit and operating loss. Management plans to eliminate the deficit and operating losses with the following actions:

The Board of Directors at the School actively focuses on a plan to reverse the accumulated deficit. The central goal of the Finance Committee is to operate the organization in a cost-sensitive manner so as to end each year with a fund surplus that can be used to repay liabilities of the School. By strengthening the effectiveness of the Business Office in providing current financial data, the Finance Committee now works pro-actively rather than re-actively on the fiscal condition of the School. Daily cash flow management projections are maintained throughout the entire school year. Monthly projections of revenues and spending are available at least 6 months in advance. All accounting records of the School are compiled and reconciled monthly under the direction of the Chairman of the Finance Committee. Compiled financial statements are discussed and approved monthly by the Board of Directors. Another key component is the growth in responsibility assumed by the Development Office at the School. Experience gained over the past four years by the Development Office has increased the ability to bring additional non-operating funds to the School. The Development Office has shown that it can creatively campaign throughout the community to bring contributions to the School despite the difficult economic climate.

As of April 2, the School has eliminated all past-due accounts payable by cutting back spending in other budgeted areas such as capital expenditures and technology. In addition, the School also paid off the \$10,000 loan received from a board member on July 15, 2003, and has plans to repay \$30,000 of the Sky Bank note by June 30, 2004. The School has also reduced expenditures made for continuous improvement of their facility. This is due to the resolution passed by the School to move their facility for the upcoming school year. Through continued cash management, budgeting, monitoring of expenditures, and repayment of debt, the School is actively working to eliminate the deficit.

19. RELATED PARTIES

A Board Member made two separate loans of \$10,000 each to the School in the year ended 2002 (See Note 15). One payment in the amount of \$10,000 was made on the loans in the year ended 2003 and another payment in the amount of \$10,000 was made on the loans in the year ended 2004.



**Auditor of State
Betty Montgomery**

**INDEPENDENT ACCOUNTANTS' REPORT ON COMPLIANCE AND ON
INTERNAL CONTROL REQUIRED BY *GOVERNMENT AUDITING STANDARDS***

Toledo School for the Arts
Lucas County
425 Jefferson Avenue
Toledo, Ohio 43604-1060

To the Governing Board:

We have audited the financial statements of the Toledo School for the Arts, Lucas County, (the School) as of and for the year ended June 30, 2003, and have issued our report thereon dated April 2, 2004. Our report expressed substantial doubt as to the ability of the School to continue as a going concern. 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 *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the School's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on 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 such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*. However, we noted a certain immaterial instance of noncompliance that we have reported to the management of the School in a separate letter dated April 2, 2004.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the School's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial

reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the School's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. A reportable condition is described in the accompanying schedule of findings as item 2003-001.

A material weakness is a 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 in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we consider the reportable condition described above to be a material weakness. We also noted other matters involving the internal control over financial reporting that do not require inclusion in this report, that we have reported to the management of the School in a separate letter dated April 2, 2004.

This report is intended for the information and use of the audit committee, management, the Governing Board, and the Sponsor, and is not intended to be and should not be used by anyone other than these specified parties.



Betty Montgomery
Auditor of State

April 2, 2004

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

**SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2003**

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

FINDING NUMBER 2003-001

Material Weakness – Purchasing

Fifty-five percent of the checks examined were paid for past-due amounts from as far back as October of 1999.

Paying bills promptly is an important aspect of financial management. It is a key control in the disbursement process to determine that expenditures are within budget and additional charges are not being incurred.

Failure to pay bills in a timely manner could result in additional charges (i.e., finance charges, late fees) having to be paid by the School. It also could result in collection disputes and could lead to disbursements exceeding budgeted amounts.

We recommend the School pay all bills in a timely manner.

**TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY**

**SCHEDULE OF PRIOR AUDIT FINDINGS
JUNE 30, 2003**

Finding Number	Finding Summary	Fully Corrected?	Not Corrected, Partially Corrected; Significantly Different Corrective Action Taken; or Finding No Longer Valid; <i>Explain:</i>
2002-001	ORC § 3314.08(J) debt maturity date extends beyond end of fiscal year.	Yes	
2002-002	Material Weakness – Purchasing: Fiscal Agent was not reviewing and signing every Purchase Order prior to a check being paid to a vendor.	Yes	



**Auditor of State
Betty Montgomery**

88 East Broad Street
P.O. Box 1140
Columbus, Ohio 43216-1140

Telephone 614-466-4514
800-282-0370

Facsimile 614-466-4490

TOLEDO SCHOOL FOR THE ARTS

LUCAS 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 4, 2004**