McGladrey & Pullen
Certified Public Accountants

# Harriet Tubman Charter School

Financial Report

June 30, 2009

# HARRIET TUBMAN CHARTER SCHOOL

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## June 30, 2009

McGladrey & Pullen
Certified Public Accountants

**Independent Auditor's Report**

To the Board of Trustees
Harriet Tubman Charter School
Bronx, New York

We have audited the accompanying statements of financial position of Harriet Tubman Charter School (the "School") as of June 30, 2009 and 2008, and the related statements of activities, functional expenses, and cash flows for the years then ended. 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 audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. 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 disclosure 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 audits provide 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, 2009 and 2008, and the change in its net assets and its cash flows for the years 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 October 29, 2009, on our consideration of the School's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contract and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and on compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

McGladrey & Pullen, LLP

New York, New York
October 29, 2009

# HARRIET TUBMAN CHARTER SCHOOL

## STATEMENT OF FINANCIAL POSITION

| June 30, | 2009 | 2008 |
|---|---|---|
| **ASSETS** | | |
| Cash | $1,895,167 | $2,161,722 |
| Cash - restricted | 75,000 | 37,500 |
| Grants Receivable, net of allowance for doubtful accounts of $8,607 and $184,530, respectively | 135,612 | 164,223 |
| Deferred Lease Premium, net | 850,000 | 935,000 |
| Property and Equipment, net | 200,616 | 111,121 |
| Other Assets | 65,637 | 75,919 |
| **Total Assets** | $3,222,032 | $3,485,485 |
| **LIABILITIES AND NET ASSETS DEFICIENCY** | | |
| Liabilities: | | |
| Accounts payable and accrued expenses | $ 52,424 | $ 12,305 |
| Refundable advances | 318,852 | 143,110 |
| Due to management company | 1,926,272 | 2,737,515 |
| Deferred rent | 132,640 | 130,491 |
| Loan payable | 20,611 | 158,364 |
| Mortgage payable - management company | 791,539 | 1,128,545 |
| **Total liabilities** | 3,242,338 | 4,310,330 |
| Commitments and Contingency | | |
| Net Assets (Deficiency): | | |
| Unrestricted: | | |
| Other | (120,572) | (887,549) |
| Board-designated | 75,000 | 37,500 |
| Temporarily restricted | 25,266 | 25,204 |
| **Net assets deficiency** | (20,306) | (824,845) |
| **Total Liabilities and Net Assets Deficiency** | $3,222,032 | $3,485,485 |

See Notes to Financial Statements

# HARRIET TUBMAN CHARTER SCHOOL

## STATEMENT OF ACTIVITIES

| Year ended June 30, | 2009 | 2008 |
| --- | --- | --- |
| Unrestricted net assets: | | |
| Operating revenue: | | |
| State and local per pupil operating revenue | $5,571,453 | $4,818,421 |
| Government grants and contracts | 618,463 | 350,214 |
| Total operating revenue | 6,189,916 | 5,168,635 |
| Operating expenses: | | |
| Program services | 3,293,316 | 3,263,248 |
| Management and general | 2,137,240 | 1,700,285 |
| Fund-raising | 12,531 | 1,590 |
| Total operating expenses | 5,443,087 | 4,965,123 |
| Net revenue from School operations | 746,829 | 203,512 |
| Contributions | 30,808 | 17,662 |
| Other income | 26,840 | 991,918 |
| Change in unrestricted net assets | 804,477 | 1,213,092 |
| Temporarily restricted net assets: | | |
| Other | 62 | 1,012 |
| Change in temporarily restricted net assets | 62 | 1,012 |
| Change in net assets | 804,539 | 1,214,104 |
| Net asset deficiency at beginning of year | (824,845) | (2,038,949) |
| Net asset deficiency at end of year | $ (20,306) | $ (824,845) |

See Notes to Financial Statements

# HARRIET TUBMAN CHARTER SCHOOL

## STATEMENT OF FUNCTIONAL EXPENSES

**Year ended June 30, 2009**

| | Program Services | Management and General | Fund-raising | Total |
|---|---|---|---|---|
| Salaries and wages | $1,796,812 | $ 702,721 | | $2,499,533 |
| Payroll taxes and employee benefits | 149,244 | 65,437 | | 214,681 |
| Equipment | 42,001 | 6,850 | | 48,851 |
| Subscriptions | 610 | 1,948 | | 2,558 |
| Contracted services | 220,510 | 13,680 | | 234,190 |
| Occupancy | 426,080 | 25,617 | | 451,697 |
| Supplies | 18,160 | 12,405 | | 30,565 |
| Instructional materials | 158,093 | 15,960 | | 174,053 |
| Telephone and Internet | 19,836 | 30 | | 19,866 |
| Insurance | 19,045 | | | 19,045 |
| Food | | 10,485 | | 10,485 |
| Employee recruiting | 31,282 | 164 | | 31,446 |
| Field trips | 11,081 | | | 11,081 |
| Staff development | 7,334 | 485 | | 7,819 |
| Interest expense | 132,929 | 7,606 | | 140,535 |
| Utilities | 87,016 | | | 87,016 |
| Assessments | 8,118 | | | 8,118 |
| Management fee | | 934,553 | | 934,553 |
| Miscellaneous | 8,031 | 8,932 | | 16,963 |
| Professional fees | | 260,957 | | 260,957 |
| Other | 47,237 | 36,487 | $12,531 | 96,255 |
| Depreciation and amortization | 109,897 | 32,923 | | 142,820 |
| Total operating expenses | $3,293,316 | $2,137,240 | $12,531 | $5,443,087 |

See Notes to Financial Statements

# HARRIET TUBMAN CHARTER SCHOOL

## STATEMENT OF FUNCTIONAL EXPENSES

**Year ended June 30, 2008**

| | Program Services | Management and General | Fund-raising | Total |
|---|---|---|---|---|
| Salaries and wages | $1,546,993 | $ 481,280 | | $2,028,273 |
| Payroll taxes and employee benefits | 575,770 | 129,580 | | 705,350 |
| Equipment | 67,665 | | | 67,665 |
| Subscriptions | 5,674 | | | 5,674 |
| Contracted services | 188,180 | 72,046 | | 260,226 |
| Occupancy | 345,531 | 4,089 | | 349,620 |
| Supplies | 4,664 | 17,696 | $1,590 | 23,950 |
| Instructional materials | 77,844 | | | 77,844 |
| Telephone and Internet | | 19,850 | | 19,850 |
| Insurance | 18,130 | 184 | | 18,314 |
| Food | | 16,730 | | 16,730 |
| Employee recruiting | | 7,549 | | 7,549 |
| Field trips | 12,030 | | | 12,030 |
| Staff development | 8,888 | | | 8,888 |
| Postage | | 2,834 | | 2,834 |
| Interest expense | 152,789 | 16,977 | | 169,766 |
| Utilities | 83,803 | 847 | | 84,650 |
| Fees | | 20,152 | | 20,152 |
| Assessments | 8,316 | | | 8,316 |
| Management fee | | 813,390 | | 813,390 |
| Miscellaneous | | 38,835 | | 38,835 |
| Professional fees | | 57,150 | | 57,150 |
| Other | 59,611 | | | 59,611 |
| Depreciation and amortization | 107,360 | 1,096 | | 108,456 |
| Total operating expenses | $3,263,248 | $1,700,285 | $1,590 | $4,965,123 |

# HARRIET TUBMAN CHARTER SCHOOL

## STATEMENT OF CASH FLOWS

| Year ended June 30, | 2009 | 2008 |
|---|---|---|
| Cash flows from operating activities: | | |
| Change in unrestricted net assets | $ 804,539 | $1,214,104 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | | |
| Depreciation and amortization | 142,820 | 108,456 |
| Bad debt expense | 16,486 | |
| Accrued interest added to mortgage payable - management company | 131,269 | 154,571 |
| Changes in operating assets and liabilities: | | |
| Decrease (increase) in grants receivable | 12,125 | (20,995) |
| Decrease (increase) in other assets | 10,282 | (31,019) |
| Increase in accounts payable and accrued expenses | 40,119 | 12,305 |
| Increase in refundable advances | 175,742 | 26,391 |
| (Decrease) increase in due to management company | (811,243) | 1,076,996 |
| Increase in deferred rent | 2,149 | 26,191 |
| **Net cash provided by operating activities** | 524,288 | 2,567,000 |
| Cash used in investing activity - purchase of property and equipment | (147,315) | (88,376) |
| Cash flows from financing activities: | | |
| Repayment of principal on loan | (137,753) | (109,467) |
| Repayment of principal on mortgage payable - management company | (468,275) | (244,799) |
| Increase in restricted cash | (37,500) | (37,500) |
| **Cash used in financing activities** | (643,528) | (391,766) |
| Net increase (decrease) in cash | (266,555) | 2,086,858 |
| Cash at beginning of year | 2,161,722 | 74,864 |
| Cash at end of year | $1,895,167 | $2,161,722 |

**Supplemental Information:**

| | 2009 | 2008 |
|---|---|---|
| Interest paid | $ 140,535 | $ 169,766 |

See Notes to Financial Statements

**1. PRINCIPAL BUSINESS ACTIVITY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:**

Harriet Tubman Charter School (the "School") is an educational corporation that operates in the borough of Bronx, New York. On January 13, 2000, the Board of Regents of the University of the State of New York granted the School a provisional charter valid for a term of five years and renewable upon expiration. In January 2005, the charter was renewed for a period of two years expiring on June 30, 2007. Upon expiration of the second renewal, the charter was again renewed for a period of two years expiring on June 30, 2009. Upon expiration of the third renewal, the charter was once again renewed for a period of two years expiring on June 30, 2011.

The School is exempt from federal income taxes under Section 501(c)(3) of the Internal Revenue Code.

The School is designed to help students develop the skills to become leaders who read, think, write and communicate at high levels. The School's mission is to prepare students for success throughout their college years and beyond.

In fiscal years 2009 and 2008, the School operated classes for students in kindergarten and grades one through eight.

The New York City Department of Education provides free lunches and transportation directly to a majority of the School's students.

The financial statements of the School have been prepared on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America.

The School reports gifts of cash and other assets as restricted support if they are received with donor stipulations that limit the use of the donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose restriction is accomplished, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of activities as net assets released from restrictions. The School reports amounts received with donor stipulations that limit the use of the assets for certain purposes as unrestricted net assets if the stipulated purpose restriction is accomplished in the same year. Contributions of assets other than cash are recorded at their estimated fair value.

Grants receivable are reported at their outstanding unpaid principal balances reduced by an allowance for doubtful accounts. The School estimates doubtful accounts based on historical bad debt, factors related to specific donors' ability to pay and current economic trends. The School writes off receivables against the allowance when a balance is determined to be uncollectible.

Revenue from the state and local government resulting from the School's charter status is based on the number of students enrolled, and is recorded when services are performed in accordance with the charter agreement.

Revenue from federal, state and local government grants and contracts are recognized by the School when qualifying expenditures are incurred and billable to the government.

The School recognizes contributed services in accordance with Statement of Financial Accounting Standards ("SFAS") No. 116, *Accounting for Contributions Received and Contributions Made.* Accordingly, contributed services are recognized as revenue and assets or expenses at fair value if those services (a) create or enhance nonfinancial assets, (b) would typically need to be purchased by the School if they had not been provided by contribution, or (c) require specialized skills and are provided by individuals with those skills.

The School maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. The School has not experienced any losses in these accounts.

Property and equipment is recorded at cost. Major additions and improvements or betterments with an estimated useful life of more than one year are capitalized. Depreciation is computed using the straight-line method over the estimated useful lives of the assets.

The School recognizes rent expense on a straight-line basis over the term of the lease. Expenses in excess of payments are recorded as deferred rent.

Expenses are classified according to the functional categories for which they are incurred, as follows:

<u>Program Services</u> - represents expenses directly associated with general education and special education for certain students requiring additional attention and guidance.

<u>Management and General</u> - represents expenses related to the overall administration and operation of the School that are not associated with any program services.

<u>Fund-raising</u> - represents expenses associated with the School's fund-raising efforts including but not limited to annual mailings, donor meetings and events.

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

The Financial Accounting Standards Board (the "FASB") has issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109* ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 prescribes a recognition threshold and measurement standard for the financial statement recognition and measurement of an income tax position taken or expected to be taken on a tax return including positions that an organization is exempt from income taxes or not subject to income taxes on unrelated business income. In addition, FIN 48 provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

The School presently discloses or recognizes income tax positions based on management's estimate of whether it is reasonably possible or probable, respectively, that a liability has been incurred for unrecognized income tax benefits by applying FASB Statement No. 5, *Accounting for Contingencies.*

The School has elected to defer the application of FIN 48 in accordance with FASB Staff Position ("FSP") FIN 48-3. This FSP defers the effective date of FIN 48 for nonpublic enterprises included within its scope to the annual financial statements for fiscal years beginning after December 15, 2008. The School will be required to adopt FIN 48 in its 2010 annual financial statements. The provisions of FIN 48 are to be applied to all tax positions upon initial application of this standard. Only tax positions that meet the more-likely-than-not recognition threshold at the effective date may be recognized or continue to be recognized upon adoption.

The cumulative effect of applying the provisions of FIN 48 will be reported as an adjustment to the opening balance of net assets for the fiscal year of adoption. Management has evaluated the effects of FIN 48 and does not expect it to have a material impact on the School's financial position and results of operations.

The School evaluates events occurring after the date of the financial statements to consider whether or not the impact of such events needs to be reflected or disclosed in the financial statements. Such evaluation is performed through the date the financial statements are available for issuance, which was October 29, 2009 for these financial statements.

## 2. PROPERTY AND EQUIPMENT, NET:

Property and equipment, net, at cost, consists of the following:

| June 30, | 2009 | 2008 | Estimated Useful Life |
|---|---|---|---|
| Leasehold improvements | $ 95,666 | $ 61,405 | 10 to 15 years |
| Computer and equipment | 105,726 | 17,439 | 3 years |
| Furniture and fixtures | 34,300 | 9,533 | 7 years |
| Playground | 97,000 | 97,000 | 8 years |
| | 332,692 | 185,377 | |
| Less accumulated depreciation | 132,076 | 74,256 | |
| | $200,616 | $111,121 | |

Depreciation expense for the years ended June 30, 2009 and 2008 was $57,820 and $23,457, respectively.

**3. LOAN PAYABLE:**

The principal sum of the loan payable was $525,000 and is payable in 60 equal monthly installments with interest at 7% per annum starting November 1, 2004. The principal balance of the loan amounted to $20,611 and $158,364 as at June 30, 2009 and 2008, respectively.

**4. MORTGAGE PAYABLE:**

On July 26, 2004, the School took a mortgage loan of $1,124,370 from Edison Learning Inc. ("Edison"), its management company, to primarily finance the lease premium payable for the leased facilities. Effective June 30, 2008, the School amended the agreement with Edison. The loan is payable on June 30, 2014 or such other earlier date on which the loan may be required to be repaid pursuant to the terms and provisions of the note, with interest at 12% per annum, and is secured by the School's interest in the leased property. Generally, payments are only required if there is available cash flows from operations of the School. The balance of the loan as of June 30, 2009 and 2008 was $791,539 and $1,128,545, respectively. The balance at June 30, 2009 and 2008 included unpaid interest of $292,952. There was no unpaid interest at June 30, 2009.

**5. MANAGEMENT AGREEMENT:**

On July 26, 2004, the School entered into a management agreement with Edison expiring on June 30, 2010, and subsequently extended to June 30, 2014. The agreement requires Edison to manage the day-to-day operations of the School, including management of the School's financial resources. As compensation for its services and the financial risks it bears, Edison is to receive a fee equal to 15% of all external public funds received by the School. Total management fee earned by Edison in fiscal 2009 and 2008 amounted to $934,553 and $813,390, respectively.

As of June 30, 2009 and 2008, the School owed Edison $1,926,272 and $2,737,515 respectively, for unpaid cash advances and management fees.

During 2008, Edison released the School from its obligation to pay approximately $913,700 in accrued interest and management fees. The forgiveness of its obligation to pay has been recognized as other income in the financial statements.

**6. CONTINGENCY:**

Certain grants and contracts may be subject to audit by the funding sources. Such audits might result in disallowances of costs submitted for reimbursement. Management is of the opinion that such cost disallowances, if any, will not have a material effect on the accompanying financial statements. Accordingly, no amounts have been provided in the accompanying financial statements for such potential claims.

**7. TEMPORARILY RESTRICTED NET ASSETS:**

Temporarily restricted net assets consist of contributions received to benefit an endowment fund for scholarships. The assets have been invested in a certificate of deposits, the balance of which was $25,266 and $25,204 at June 30, 2009 and 2008, respectively.

**8. COMMITMENTS:**

On August 20, 2004, the School entered into a long-term lease agreement for its School facilities expiring on December 31, 2024. Future minimum lease payments under this lease are as follows:

| Year ending June 30, | |
|---|---|
| 2010 | $ 307,400 |
| 2011 | 320,270 |
| 2012 | 333,140 |
| 2013 | 333,140 |
| 2014 | 347,300 |
| Thereafter | 1,806,450 |
| | $3,447,700 |

Rent expense charged to operations amounted to approximately $321,400 and $349,600 for the years ended June 30, 2009 and 2008, respectively. Deferred rent of $132,640 and $130,491 represents an obligation for the accumulated rent expense recorded by the School from the inception of the lease in excess of the required lease payments through June 30, 2009 and 2008, respectively.

The School entered into a surrender agreement with the landlord and the previous tenant on June 30, 2004. Under the terms of the agreement, certain assets as well as a promissory note totaling $1,275,000 was provided to the landlord and the previous tenant in exchange for the release from a previous commitment from a prior lease agreement. The amount is being amortized over the life of the present lease (15 years) and, as at June 30, 2009 and 2008, the balance is $850,000 and $935,000, net of total accumulated amortization of $425,000 and $340,000 respectively.

**9. EMPLOYEE BENEFIT PLAN:**

The School is a participating employer in the Teachers' Retirement System of the City of New York ("TRS"). The amount charged to operations for contributions to TRS for the year ended June 30, 2008 was $279,406. The School received a credit of $307,796 for the year ended June 30, 2009.

McGladrey & Pullen
Certified Public Accountants

**Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards***

To the Board of Trustees
Harriet Tubman Charter School
Bronx, New York

We have audited the financial statements of Harriet Tubman Charter School (the "School") as of and for the year ended June 30, 2009, and have issued our report thereon dated October 29, 2009. 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.

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, but not for the purpose of expressing an opinion on the effectiveness of the School's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the School's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A *control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of 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 entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with accounting principles generally accepted in the United States of America such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected. We consider the deficiencies described in the accompanying schedule of findings and recommendations as item 09-01 to be significant deficiencies in internal control over financial reporting.

A *material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the School's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that none of the significant deficiencies described above is a material weakness.

Compliance and Other Matters - 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, contract and grant agreements, 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 instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* and which are described in the accompanying schedule of findings and recommendations as item 09-02.

This report is intended solely for the information and use of the audit committee, board of trustees, management, the New York State Education Department and the Board of Regents of the University of the State of New York and is not intended to be and should not be used by anyone other than these specified parties.

McGladrey & Pullen, LLP

New York, New York
October 29, 2009

## Current-Year's Findings

### 09-01 Financial Accounting and Reporting System*

Criteria

All significant accounts should be reconciled timely and regularly to ensure that financial records are accurate.

Condition

At the time of audit we found most accounts to be properly reconciled. The following were exceptions affecting significant accounts:

- The School was not able to complete its reconciliation of its accounts with EdisonLearning, Inc. until less than a week prior to the deadline for completing the financial statements. Edison initially confirmed to us an incorrect balance during the audit.

- The School did not perform a proper reconciliation of its student revenue during the year.

Cause and Effect

The accounts with Edison need to be reconciled to ensure that all costs incurred by Edison on behalf of the School are properly recorded in the School's financial records. The School recorded 12 adjusting entries to complete the reconciliation.

The revised Student Reconciliation Report for the fiscal year ended June 30, 2008 was not sent to the New York City Department of Education (the "NYCDOE"). As a result, the NYCDOE did not reduce per student advances during the year ended June 30, 2009 by the overpayments from the previous year. The School recorded a refundable advance due to the NYCDOE at June 30, 2009 of $318,812.

Recommendations

The School should develop and agree on a schedule with Edison to ensure timely and regular completion of reconciliations. Compliance with this schedule should be reported to the Finance Committee.

The School should reconcile transactions with the NYCDOE at least monthly to ensure that revenue received and recorded matches that earned for the number of students enrolled.

Management's Response

The School will resubmit immediately the revised 2008 reconciliation report to the NYCDOE. Additionally, the School will require the management company to meet quarterly to reconcile their accounts with the School to ensure that the two agree. Finally, the Chief Financial Officer will check the billings each month to approve them before they are sent, which will ensure that the Director of Operations is compliant with all reporting requirements.

* Significant deficiencies.

## Compliance and Other Matters

### 09-02 Compliance with Charter Requirements

Criteria

The School should comply with all appropriate requirements of its authorizer.

Condition

The Office of Audit Services of the New York State Education Department (the "NYSED") issued an audit report, dated June 27, 2007, covering the period from July 1, 2004 through March 28, 2006. The report contained 82 recommendations. The School's management has represented to us that most of the recommendations have been addressed; however, the following three remain as of June 30, 2009:

- Collection of lunch payments
- Annual requirement to update authorized signatories with the bank
- Tagging fixed assets

Cause and Effect

The School intended to address all 82 recommendations during the fiscal year ended June 30, 2009, but did not implement changes for three recommendations.

Recommendation

The School should ensure that it addressed the remaining recommendations of the NYSED audit report as soon as possible.

Management's Response

The School is in the process of implementing the remaining three items.

**Prior-Year's Findings**

**Internal Control Over Financial Reporting**

**08-01 Financial Accounting and Reporting System***

Criteria

Adequate internal controls should be established and maintained to ensure the reliability of an organization's financial accounting and reporting system.

Condition

At the commencement of our fieldwork, we noted that the books and records of the School were not ready for audit. We noted that prepayments and accruals at the beginning of the year were not reversed, depreciation and amortization was not recorded during the year and year-end accruals had not been recorded. We also noted the following matters, which were indicative of a failure in the School's internal controls over financial accounting and reporting:

- Major general ledger account balances were not regularly analyzed and reconciled to the supporting source documents.
- Intercompany accounts with the School's management company, EdisonLearning, Inc., were not reconciled prior to June 30, 2008.
- The School could not provide the details and backup documents to support leasehold improvements amounting to $448,567 at June 30, 2007. During the audit, it was determined that they were incorrectly accounted for and they have been eliminated by prior-period adjustment.
- A number of journal entries were not properly recorded and in some cases no supporting documentation was available to support entries.
- New York City Automate the School ("ATS") and final full time equivalent count ("FTE") reported on the student reconciliation and submitted to the New York City Board of Education ("NYCBOE") reflected a significant difference resulting from the fact that certain students were reported twice on the final reconciliation sent to the state. NYCBOE was also billed for special education students without any supporting documentation. This resulted in an overstatement of tuition revenue. An adjustment was made to correct the amount of revenue recorded.

Management, independently and in consultation with us, made approximately 21 additional journal entries in order to correct the financial statements.

Cause and Effect

Many of these conditions also existed and were reported in the audit for the previous year. The School hired a chief operating officer in 2007, who resigned in February 2008 shortly after completion of the previous audit. The School hired Kiwi Partners to provide outsourced "chief financial officer" services in June 2008. As a result, the personnel assigned to maintain the books and records of the School lacked the necessary qualifications, skills, and experience for most of the year ended June 30, 2008.

This has also adversely affected the reliability of the School's financial statements at June 30, 2008.

* Significant deficiencies and material weakness.

Recommendations

We recommend that the School maintain the improvements made to the control environment by:

- Maintaining the continuing employment of qualified and competent accounting personnel who are responsible for effectively maintaining the accounting books and records.
- Reconciling and carefully reviewing the ATS report and the final reconciliation sent to the state.
- Furthermore, we recommend that the School implement control activities such as the following:

  All significant general ledger accounts should be analyzed on a regular basis and reconciled to the supporting source documents.

  Intercompany accounts with Edison should be reconciled at least on a quarterly basis.

Current-Year's Status

In the previous year, the board indicated that it was committed to changing as a result of the previous audit. They set out to establish stronger fiscal oversight. They held monthly finance committee meetings where they have approved the monthly bank reconciliations, general journal entries made during the month and the general ledger as prepared by their staff accountant. They recruited a new member to the board, Mr. Winston Thompson of Thompson & Company CPAs and appointed him chairman of the finance committee. The school engaged Kiwi Partners as its chief financial officer ("CFO"). Kiwi has extensive experience with charter schools throughout New York City and they are managing the transition to implement a system whereby the internal books are inclusive of all transactions as original entries and thereby reduce and eventually discontinue the practice of mass journal entries to record their accounts payable transactions.

Accounts are analyzed on a quarterly basis to help ensure the fiscal integrity of the accounts.

We noted no discrepancies in the ATS report in 2009.

The Due to Edison account was reconciled more frequently than in the past. While this account did not require as much work as it did in the past, we again noted the fact that reconciling this account required much work at the time of the audit. In some cases, we noted the fact that supporting documentation was not always provided to the school on a timely basis.

See current-year's comment 09-01.

## Compliance and Other Matters

**08-02 Compliance with Charter Requirements**

Criteria

The School should comply with all appropriate requirements of its authorizer.

Condition

The School's Third Renewal Charter requires that a review be performed of the School's management and financial controls by October 1, 2007. The School has not yet had such review performed.

Furthermore, the Office of Audit Services of the NYSED issued an audit report, dated June 27, 2007, covering the period from July 1, 2004 through March 28, 2006. The report contained 82 recommendations on the following areas:

- Budgeting, accounting and reporting
- Purchasing and expenditures
- Governance and planning
- Payroll and personnel
- Revenue and cash management
- Facilities and equipment
- Student services

The School's management has agreed with 80 of the 82 recommendations and stated its intention to implement them in 2008.

Cause and Effect

The School's management was not adequately addressing these issues, some of which are separately addressed in the other comments in this report. The School risks its charter if it does not adequately address these matters.

Recommendation

The School should ensure that the required review of its management and financial controls and the appropriate recommendations of the NYSED audit report are addressed as soon as possible.

This condition was also present in 2007. The School is in the process of addressing those issues. We noted a status document indicating that the School had completed some of the tasks that would allow them to address some of the 80 recommendations.

Current-Year's Status

The School's charter was renewed in December 2008. See comment 09-02 for an update for the remaining items above.

**08-03 Maintenance of Student Records**

Criteria

Appropriate records of student enrollment and attendance should be properly maintained.

Observation

Our tests of 25 student files disclosed the following exceptions:

- No proof that the student was selected through lottery - 5 instances
- No copy of birth certificate - 1 instance
- No proof of address - 4 instances
- No student files - 2 instances

Cause and Effect

This condition is also caused by management's inability to prepare and maintain adequate records, which could adversely impact its charter.

Recommendation

All student records should be properly maintained on file for reference purposes.

Current-Year's Status

No issues were noted during the audit of the financial statements for the current year.