



**HARMONY COMMUNITY - CINCINNATI, INC.
HAMILTON COUNTY**

REGULAR AUDIT

FOR THE FISCAL YEAR ENDED JUNE 30, 1999



JIM PETRO
AUDITOR OF STATE

STATE OF OHIO

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REPORT OF INDEPENDENT ACCOUNTANTS

Harmony Community - Cincinnati, Inc.
Hamilton County
7030 Reading Road
Suite 350
Cincinnati, Ohio 45237

To the Management Cabinet:

We have audited the accompanying Balance Sheet of Harmony Community - Cincinnati, Inc., Hamilton County, Ohio, as of June 30, 1999, and the related Statement of Revenues, Expenses, and Changes in Retained Earnings, and the Statement of Cash Flows for the year then ended. These financial statements are the responsibility of Harmony Community - Cincinnati, Inc.'s management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards 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 Harmony Community - Cincinnati, Inc., Hamilton County, Ohio, as of June 30, 1999, the results of its operations, and its cash flows for the year then ended in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated March 24, 2000, on our consideration of Harmony Community - Cincinnati, Inc.'s internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

A handwritten signature in black ink, appearing to read "Jim Petro".

Jim Petro
Auditor of State

March 24, 2000

HARMONY COMMUNITY - CINCINNATI, INC.
BALANCE SHEET
AS OF JUNE 30, 1999

Assets

Current Assets:

Cash and Cash Equivalents \$569,185

Noncurrent Assets:

Furniture and Equipment Net of
accumulated depreciation 262,721

Total Assets \$831,906

Liabilities and Fund Equity

Current Liabilities:

Account Payable 116,660
Accrued Wages and Benefits 47,020
Intergovernmental Payable 24,542

Total Current Liabilities 188,222

Long-Term Liabilities:

Loan Payable 187,741

Total Liabilities 375,963

Fund Equity:

Retained Earnings:
Unreserved 455,943

Total Fund Equity 455,943

Total Liabilities and Fund Equity \$831,906

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

HARMONY COMMUNITY - CINCINNATI, INC.
STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN
RETAINED EARNINGS
FOR THE FISCAL YEAR ENDED JUNE 30, 1999

Operating Revenues:	
Foundation Payments	\$859,196
Disadvantaged Pupil Impact Aid	8,492
State Special Education Program	106,272
Other Operating Revenue	<u>2,993</u>
 Total Operating Revenues	 976,953
Operating Expenses:	
Salaries	569,091
Fringe Benefits	137,574
Purchased Services	276,311
Materials and Supplies	20,607
Depreciation	89,251
Other Operating Expenses	<u>36,367</u>
 Total Operating Expenses	 <u>1,129,201</u>
Operating Loss	<u>(152,248)</u>
Non-Operating Revenues:	
Other State Grants	590,279
Federal Grants	16,312
Interest Income	<u>1,600</u>
 Total Non-Operating Revenues	 <u>608,191</u>
Net Income	455,943
 Retained Earnings at Beginning of Year	 <u>0</u>
Retained Earnings at End of Year	<u><u>\$455,943</u></u>

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

HARMONY COMMUNITY - CINCINNATI, INC.
STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 1999

Increase (Decrease) in Cash and Cash Equivalents:

Cash Flows from Operating Activities:	
Cash Received from State of Ohio	\$973,960
Cash Payments to Employees for Services	(635,103)
Cash Payments to Suppliers for Goods and Services	(216,625)
Other Operating Revenue	<u>2,993</u>
Net Cash Provided by Operating Activities	<u>125,225</u>
Cash Flows from Noncapital Financing Activities:	
State and Federal Grants Received	<u>606,591</u>
Net Cash Provided by Noncapital Financing Activities	<u>606,591</u>
Cash Flows from Capital and Related Financing Activities:	
Acquisition of Capital Assets	(114,056)
Repayment of Loan	<u>(50,175)</u>
Net Cash Used for Capital and Related Financing Activities	<u>(164,231)</u>
Cash Flows from Investing Activities:	
Cash Received from Interest Revenue	<u>1,600</u>
Net Cash Provided from Investing Activities	<u>1,600</u>
Net Increase in Cash and Cash Equivalents	569,185
Cash and Cash Equivalents at Beginning of Year	<u>0</u>
Cash and Cash Equivalents at End of Year	<u><u>\$569,185</u></u>
<u>Reconciliation of Operating Income/(Loss) to Net Cash Provided</u>	
<u>(Used) for Operating Activities:</u>	
Operating Loss	(\$152,248)
<u>Adjustments To Reconcile Operating Loss to Net Cash Provided/</u>	
<u>(Used) for Operating Activities:</u>	
Depreciation	89,251
Changes in Assets and Liabilities:	
(Increase) Decrease in Accounts Receivable	0
(Increase) Decrease in Other Assets	0
Increase (Decrease) in Accounts Payable	116,660
Increase (Decrease) in Intergovernmental Payable	24,542
Increase (Decrease) in Accrued Wages	47,020
Increase (Decrease) in Compensated Absences Payable	<u>0</u>
Total Adjustments	<u>277,473</u>
Net Cash Provided by Operating Activities	<u><u>\$125,225</u></u>

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

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HARMONY COMMUNITY - CINCINNATI, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 1999

1. DESCRIPTION OF THE SCHOOL AND REPORTING ENTITY

Harmony Community - Cincinnati, Inc. (the School) is a nonprofit corporation established pursuant to Ohio Rev. Code Chapters 3314 and 1702 to provide an appropriate educational facility and program for all age groups and to provide instruction in courses which meet general educational requirements compatible with and approved by the State of Ohio. The School qualifies as an exempt organization under Section 501 (c) (3) of the Internal Revenue Code. The School's management is not aware of any course of action or series of events that have occurred that might adversely affect the School's exempt status. The School, which is part of the state's education program, is independent of any school district. The School may sue and be sued, acquire facilities as needed, and contract for any services necessary for the operation of the school.

The creation of the School was initially proposed to the State Board of Education of Ohio, the sponsor, by the Harmony School - Cincinnati, Inc. on June 9, 1998. The State Board of Education approved the proposal and entered into a contract with the Management Cabinet of the School. By-laws of the Corporation were amended to allow for the creation of the Management Cabinet of Harmony Community School. Members of the Cabinet were appointed by the Corporate Board of Directors. The contract provided for the commencement of School operations on September 16, 1998.

The fiscal operations of the School is under a six member Management Cabinet who was directed by the Chief Financial Officer. This Cabinet is responsible for formulating policies regarding fiscal operations and monitoring the expenditure of funds. As well, the Treasurer of the Board served as the Chief Financial Officer of the School, directed the financial affairs of the School including accounting purchasing, insurance, housekeeping and maintenance and was responsible for reporting the progress of the School against those responsibilities.

The reporting entity is composed of the primary government. The primary government of the School consists of all funds, departments, boards and agencies that are not legally separate from the School. For Harmony Community - Cincinnati, Inc., this includes Harmony Community School, The Office of Outreach Services, and the Institute for Social Research and Development. The Office of Outreach Services and the Institute for Social Research and Development were not in operation in fiscal year 1999.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of Harmony Community - Cincinnati, Inc. have been prepared in conformity with generally accepted accounting principles (GAAP) 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 (FASB) 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.

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.

HARMONY COMMUNITY - CINCINNATI, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 1999
(Continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Measurement Focus and Basics 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. 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

Unlike other public schools located in the state of Ohio, community schools are not required to follow budgetary provisions set forth in Ohio Rev. Code Chapter 5705, unless specifically provided in the School's contract with its Sponsor. The contract between the School and its Sponsor does prescribe a budgetary process for the School.

D. Cash and Cash Equivalents

All monies received by the School are accounted for by the School's Chief Financial Officer. For cash management, all cash received by the chief financial officer is pooled in a non-interest bearing central bank account. Total cash for the School is presented as "cash and cash equivalents" on the accompanying balance sheet.

The school had no investments during the fiscal year.

E. Fixed Assets and Depreciation

Fixed assets are capitalized at cost (or estimated historical 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 maintains a capitalization threshold of two hundred dollars. 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 and equipment is computed using the straight-line method over and estimated useful life of five years. Improvements to fixed assets are depreciated over the remaining useful lives of the related fixed assets.

HARMONY COMMUNITY - CINCINNATI, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 1999
(Continued)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

F. Intergovernmental Revenues

The School currently participates in the State Foundation Program, the State Disadvantaged Pupil Impact Aid (DPIA) Program, and the State Special Education Program. These programs are recognized as operating revenues in the accounting period in which they are earned and become measurable.

Grants and entitlements are recognized as non-operating revenues in the accounting period in which they are earned and became measurable.

G. 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 unused vacation time when earned for all employees.

Sick leave benefits are accrued as a liability using the termination method. An accrual for earned sick leave is made to the extent that it is probable that benefits will result in termination payments.

At June 30, 1999, compensated absences is immaterial to the financial statements.

H. Accrued Liabilities

Obligations, such as accrued wages and benefits, are reported as liabilities in the accompanying financial statements.

3. CASH AND DEPOSITS

At June 30, 1999 the school had a cash balance of \$569,185 which is presented as a cash and cash equivalents in the accompanying financial statements. The bank balance of the School's deposits was \$620,123 of which \$100,000 was covered through federal depository insurance (FDIC), and \$520,123 is uninsured and uncollateralized.

4. FIXED ASSETS

A summary of the Enterprise Fund fixed assets at June 30, 1999:

Furniture and Equipment	\$351,972
Less: Accumulated Depreciation	<u>(89,251)</u>
Net Fixed Assets	<u>\$262,721</u>

HARMONY COMMUNITY - CINCINNATI, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 1999
(Continued)

5. 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 fiscal year 1999, the School contracted with EMC Insurance Companies for property and general liability insurance. There is a \$1,000 deductible with a one hundred percent blanket, all risk policy.

B. Employee Medical, Dental, and Vision Benefits

The School has contracted with a private carrier to provide employee medical/surgical benefits. The School pays 100% of the monthly premium

6. OPERATING LEASE

The School has a month-to-month lease with Allen Temple Real Estate Foundation for 37,000 square feet of building space to be used for educational purposes. In fiscal year 1999, the School paid \$5,000 per month, plus \$297 per month for each child above a census of 175 students. At June 30, 1999, the School paid \$52,300, and had a payable of \$61,000.

7. 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 public employee retirement system administered by the School Employees Retirement Board. SERS provides basic retirement benefits, disability, survivor, and health care benefits based on eligible service credit to members and beneficiaries. Benefits are established by Chapter 3309 of the Ohio Revised Code. SERS issues a publicly available financial report that includes financial statements and required statements and required supplementary information for SERS. That report may be obtained by writing to the School Employees Retirement System, 45 North Fourth Street, Columbus, Ohio 43215-3634.

Plan members are required to contribute 9 percent of their annual covered salary and the School is required to contribute 14 percent; for fiscal year 1999, 7.7 percent was the portion to fund pension obligations. The contribution rates are established by SERS's Retirement Board within the rates allowed by State statute. The School's required contribution for pension obligations to SERS for the fiscal year ended June 30, 1999 was \$11,324; 71 percent has been contributed for fiscal year 1999. \$3,297 representing the unpaid contributions for fiscal year 1999, is recorded as a liability.

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 basic retirement benefits, disability, survivors, and health care benefits based on eligible service credit to members and 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 for STRS. That report may be obtained by writing to the State Teachers Retirement System, 275 East Broad Street, Columbus, Ohio 43215-3771.

HARMONY COMMUNITY - CINCINNATI, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 1999
(Continued)

7. DEFINED BENEFIT PENSION PLANS (Continued)

Plan members are required to contribute 9.3 percent of their annual covered salary and the School is required to contribute 14 percent; 6 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 contribution for pension obligation to STRS for the fiscal year ended June 30, 1999 was \$22,535; 72 percent has been contributed for fiscal year 1999. \$6,225 representing the unpaid contributions for fiscal year 1999, is recorded as a liability.

C. Social Security System

Effective July 1, 1991, all employees not otherwise covered by the School Employees Retirement System or the State Teachers Retirement System have an option to choose Social Security or the School Employees Retirement System/State Teacher Retirement System. As of June 30, 1999, the School has no employees or members of the governing board who contribute to Social Security.

8. 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-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 System based on authority granted by State statute. Both systems are on a pay-as-you-go basis.

For STRS, all benefit recipients are required to pay a portion of health care cost in the form of a monthly premium. By Ohio Law, the cost of coverage paid from STRS funds shall be included in the employer contribution rate, currently 14 percent of covered payroll. The board currently allocates employer contributions equal to 8 percent of covered payroll to the Health Care Reserve Fund from which payments for health care benefits are paid. For the School, this amount equaled \$30,047 during the 1999 fiscal year.

STRS pays health care benefits from the Health Care Reserve Fund. At June 30, 1998 (the latest information available) the balance in the Fund was \$2,156 million. For the year ended June 30, 1998, net health care costs paid by STRS were \$219,224,000 and STRS had 91,999 eligible benefit recipients.

For SERS, coverage is made available to service retirees with ten or more fiscal 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 this fiscal year, employer contributions to fund health care benefits were 6.3 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 1999, the minimum pay has been established at \$12,400. For the School, the amount to fund health care benefits, including surcharge, equaled \$9,265 during the 1999 fiscal year.

The surcharge, added to the unallocated portion of the 14 percent employer contribution rate, provides for maintenance of the asset target level for the health care fund. The target level for the health care reserve is 125 percent of annual health care expenses. Expenses for health care at June 30, 1998 (the latest information available), were \$111,900,575 and the target level was \$139.9 million. At June 30, 1998, SERS had net assets available for payment of health care benefits of \$160.3 million. SERS has approximately 50,000 participants currently receiving health care benefits.

HARMONY COMMUNITY - CINCINNATI, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 1999
(Continued)

9. Other Employee Benefits

A. Compensated Absences

The criteria for determining vacation and sick leave components are derived from school policies and State Laws. Full-time employees are eligible for fifteen days of paid vacation each year. Employees may not carry more than twenty five days of accrued vacation at any one time.

This is the first year the School is in operation and there is no policy on the accrual and payment of sick leave.

B. Insurance Benefits

The School District provides life insurance to all employee through a private carrier. Coverage is provided for all certified and noncertified employees.

10. DEBT

During fiscal year 1999, the Treasurer entered into a loan with Firststar Bank with a limit of \$275,000 at an interest rate of 7 percent. As of June 30, 1999, \$237,916 was borrowed against the limit. The agreement allows the school to purchase or lease equipment and make payments to the bank in monthly installments. As of June 30, 1999, \$50,175 was paid in principal. The following is a summary of the District's future annual debt payments:

<u>Fiscal Year</u> <u>Ending June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2000	\$102,418	\$13,142	\$115,560
2001	<u>85,323</u>	<u>5,973</u>	<u>91,296</u>
	<u>\$187,741</u>	<u>\$19,115</u>	<u>\$206,856</u>

The debt is not evidenced by notes and does not mature at fiscal year end. State law requires that debt be evidenced by notes that mature by fiscal year end.

11. STATE SCHOOL FUNDING DECISION

On March 24, 1997, the Ohio Supreme Court rendered a decision declaring certain portions of the Ohio school funding plan unconstitutional. The Court stayed the effect of its ruling for one year to allow the State's legislature to design a plan to remedy the perceived defects in the system. Declared unconstitutional was the State's school foundation program which provides significant amounts of monetary support to the School. During the fiscal year ended June 30, 1999, the School District received \$859,196 of school foundation support for its operations.

Since the Supreme Court ruling, numerous pieces of legislation have been passed by the Ohio General Assembly in an attempt to address the issues identified by the Court. The Court of Common Pleas in Perry County has reviewed the new laws and, in a decision issued on February 26, 1999, determined they are not sufficiently responsive to the constitutional issues raised under the "thorough and efficient", clause of the Ohio Constitution. The State has appealed the decision made by the Court of Common Pleas to the Ohio Supreme Court. At this time, the Ohio Supreme Court has not rendered an opinion on this issue. The decision of the Court of Common Pleas in Perry County has been stayed by the Ohio Supreme Court, and, as such, schools are still operating under the laws that the Common Pleas Court declared unconstitutional.

HARMONY COMMUNITY - CINCINNATI, INC.
NOTES TO THE FINANCIAL STATEMENTS
JUNE 30, 1999
(Continued)

11. STATE SCHOOL FUNDING DECISION (Continued)

As of the date of these financial statements, the School is unable to determine what effect, if any, this ongoing litigation will have on its future State funding under this program and on its financial operations.

12. CONTINGENCIES

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 is subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the general fund or other applicable 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, 1999.

13. SUBSEQUENT EVENTS

During fiscal year 1999, there was a contractual dispute with Cincinnati Bell Supply Company regarding payment for computer equipment that the School considered defective. The School agreed to pay \$15,000 which Cincinnati Bell Supply Company accepted as payment in full for this equipment. At June 30, 1999, the \$15,000 is shown as a payable on the financial statements.

14. RELATED PARTIES

During fiscal year 1999, the husband of a cabinet member of the School was the Director of Harmony Community - Cincinnati, Inc. This Cabinet member was also employed by the School.

During fiscal year 1999, Harmony Community - Cincinnati, Inc. purchased property and liability insurance through the President of the Management Cabinet who is an insurance agent. Expenses recognized with this transaction are \$4,170.

15. MATERIAL NONCOMPLIANCE

The School could not locate records that State law required them to maintain.

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

Harmony Community - Cincinnati, Inc.
Hamilton County
7030 Reading Road
Suite 350
Cincinnati, Ohio 45237

To the Management Cabinet:

We have audited the financial statements of Harmony Community - Cincinnati, Inc., Hamilton County, Ohio, as of and for the fiscal year ended June 30, 1999, and have issued our report thereon dated March 24, 2000. We conducted our audit in accordance with generally accepted auditing standards 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 Harmony Community - Cincinnati, Inc.'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 instances of noncompliance that are required to be reported under *Government Auditing Standards* as item 1999-10431-001 through 1999-10431-002.

We also noted certain immaterial instances of noncompliance that we have reported to management of Harmony Community - Cincinnati, Inc. in a separate letter dated March 24, 2000.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Harmony Community - Cincinnati, Inc.'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 certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. 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 Harmony Community - Cincinnati, Inc.'s ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying Schedule of Findings as items 1999-10431-003 and 1999-10431-004.

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, of the reportable conditions described above, we consider item 1999-10431-003 to be a material weakness.

We also noted other matters involving the internal control over Harmony Community - Cincinnati, Inc. Hamilton County financial reporting that do not require inclusion in this report, that we have reported to management of Harmony Community - Cincinnati, Inc. in a separate letter dated March 24, 2000.

This report is intended for the information and use of the management and the Management Cabinet, and is not intended to be and should not be used by anyone other than these specified parties.

A handwritten signature in black ink, appearing to read "Jim Petro", with a large, stylized flourish at the end.

Jim Petro
Auditor of State

March 24, 2000

**SCHEDULE OF FINDINGS
JUNE 30, 1999**

FINDINGS RELATED TO THE FINANCIAL STATEMENTS REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS
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FINDING NUMBER 1999-10431-001

Noncompliance Citation

Ohio Rev. Code, Section 149.351, provides that no public records shall be removed, destroyed, mutilated, transferred, or otherwise damaged or disposed of, in whole or in part, except as provided by law or under the rules adopted by the records commission provided for under Ohio Rev. Code Section 149.38 to 149.42. The School was unable to locate the following items: seven invoices, federal and state withholding forms for seven employees, retirement authorization forms for eight employees, personnel files for three employees, four federal quarterly tax returns, and July 1998 through May 1999 payroll and nonpayroll bank reconciliations.

Without proper documentation, assets could be misappropriated, there could be material misstatements in the financial statements, or unauthorized or overpayment of invoices or payroll could occur.

We recommend the School maintain all supporting documentation and keep all documentation in a secure location.

FINDING NUMBER 1999-10431-002

Noncompliance Citation

Ohio Rev. Code , Section 3314.08(J), states a community school may borrow money to pay any necessary and actual expenses of the school in anticipation of the receipt of any portion of the payments to be received by the school pursuant to division (D) of this section. The school may issue notes to evidence such borrowing to mature no later than the end of the fiscal year in which such money was borrowed. The proceeds of the notes shall be used only for the purposes for which the anticipated receipts may be lawfully expended by the school. The School has a loan with Firststar Bank for the purchase and lease of equipment, but it is not evidenced by notes and it did not mature by fiscal year end.

We recommend the School obtain notes to pay the loan and pay it by fiscal year 2000.

FINDING NUMBER 1999-10431-003

Reportable Condition/Material Weakness

Payroll Processing Procedures

The following control weaknesses were noted in the system for processing payroll:

- None of the employees were approved for hire through the Management Cabinet, nor was the established pay rate for the positions approved.
- No documentation was provided for hourly employees showing hours worked and supervisory approval.
- There was no documentation of attendance for salaried employees during the fiscal year.
- No review of the payroll spreadsheets prepared by the Treasurer was documented by the Director.
- Records were not maintained indicating leave accruals or leave time taken during the fiscal year.

SCHEDULE OF FINDINGS
JUNE 30, 1999
(Continued)

FINDINGS RELATED TO THE FINANCIAL STATEMENTS REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS (Continued)
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FINDING NUMBER 1999-10431-003

Reportable Condition/Material Weakness

Payroll Processing Procedures (Continued)

This required the Management Cabinet to retroactively approve the salaries for the fiscal year 1999. Had we not been able to obtain this subsequent documentation from the Management Cabinet, it may have resulted in a scope limitation. Due to this, we deemed this to be a material weakness in their controls over payroll procedures. Failure to establish a favorable control environment could result in a material misstatement, overpayment, or unauthorized payment relating to payroll expenditures to occur.

The following procedures should be applied to help ensure a favorable control environment and to aid in identifying misstatements either as they occur or through the review process:

- Approval through the Management Cabinet to hire all employees of the School;
- Approval through the Management Cabinet of all pay rates;
- Review process to ensure all employees' gross wages as paid agree to the approved pay rate;
- Process requiring all wages paid to hourly (non-salary) employees to be adequately supported by a time sheet documenting hours worked and which has been appropriately approved by someone with sufficient knowledge to verify the hours worked;
- Review process of attendance of salaried employees;
- Approval through the Management Cabinet for all pay rate increases; and
- Maintain records for employees showing leave accrued and leave used and documentation that the records are reviewed by the Director.

In July 1999, the School contracted with an outside payroll company for payroll processing.

FINDING NUMBER 1999-10431-004

Reportable Condition

Purchasing Cycle

The following control weaknesses were noted in the purchasing process control environment:

- There was no prior authorization of purchases by the Director.
- Invoices, copy of the checks, and any other pertinent information were not filed together.
- The checks were not signed by two authorized signatories.
- The invoice was not initialed by the receiver before payment of the invoice.
- No review process is in place by management to ensure that the expenditure was appropriately

posted to the proper account.

**SCHEDULE OF FINDINGS
JUNE 30, 1999
(Continued)**

FINDINGS RELATED TO THE FINANCIAL STATEMENTS REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS (Continued)
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FINDING NUMBER 1999-10431-004

Reportable Condition

Purchasing Cycle (Continued)

- Unused checks were not kept locked in a cabinet.

These control weaknesses could result in errors or misstatements in the financial records, the unauthorized purchase of goods or services, or the misappropriation of school assets. The school has implemented policies and procedures related to purchasing controls, but are not following their established procedures.

A favorable control environment for the processing of non-payroll disbursements may include, but are not limited to:

- Prior authorization of a purchase, through the use of a purchase order which should be approved and documented through appropriate members of management and which should include appropriate coding of the expenditures;
- Accumulation of appropriate supporting documentation (original invoices) prior to authorization for payment;
- Detailed review of the invoice and supporting documentation indicating descriptions of the goods/services received and documentation on the invoice that the goods/services were received ("okay to pay");
- Matching of invoice with purchase order and copy of check or check stub to ensure all supporting documentation has been reviewed;
- Review of check used to pay the purchase and supporting documentation to ensure that the payee, amount, address, etc. on the check and invoice agree;
- Review of expenditures as posted to the expenditure ledger to ensure appropriate coding was utilized for payment, and
- Storage of unused checks should be maintained in a secure location.



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HARMONY COMMUNITY - CINCINNATI, INC.

HAMILTON 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
APRIL 18, 2000**