HARMONY COMMUNITY - CINCINNATI, INC.
HAMILTON COUNTY

REGULAR AUDIT

FOR THE YEAR ENDED JUNE 30, 2002

Auditor of State
Betty Montgomery

HARMONY COMMUNITY – CINCINNATI, INC.
HAMILTON COUNTY

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Auditor of State
Betty Montgomery

INDEPENDENT ACCOUNTANTS' REPORT

Harmony Community – Cincinnati, Inc.
Hamilton County
1580 Summit Road
Cincinnati, Ohio 45237

To the Management Cabinet:

We have audited the accompanying balance sheet of the Harmony Community – Cincinnati, Inc., Hamilton County, Ohio (the School), as of June 30, 2002, and the related Statement of Revenues, Expenses, and Changes in Accumulated Deficit/Retained Earnings, and the Statement of Cash Flows for the year 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 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 Harmony Community - Cincinnati, Inc., Hamilton County, Ohio (the School), as of June 30, 2002, 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 School has a working capital deficiency of $83,106. Management's plan in regard to this matter is described in Note 17. 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 September 12, 2003, 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

Betty Montgomery
Auditor of State

September 12, 2003

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HARMONY COMMUNITY-CINCINNATI, INC.
HAMILTON COUNTY

BALANCE SHEET
AS OF JUNE 30, 2002

Assets		
Current Assets		
Cash	$	203,975
Cash on Hand		203
Security Deposits		127,045
Prepaid Items		69,062
Total Current Assets		400,285
Noncurrent Assets		
Capital Assets (Net of accumulated depreciation)		191,530
Total Noncurrent Assets		191,530
Total Assets	$	591,815
Liabilities and Fund Equity		
Current Liabilities		
Account Payable	$	143,772
Accrued Payables		74,000
Capital Lease Payable		7,393
Accrued Wages and Benefits		16,648
Intergovernmental Payable		33,719
Short-Term Loans Payable		5,949
Line of Credit Payable		201,910
Total Current Liabilities		483,391
Noncurrent Liabilities		
Capital Lease Payable		4,700
Total Liabilities		488,091
Fund Equity		
Retained Earnings Unreserved		103,724
Total Fund Equity		103,724
Total Liabilities and Fund Equity	$	591,815

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

HARMONY COMMUNITY-CINCINNATI, INC.
HAMILTON COUNTY

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN ACCUMULATED DEFICIT/RETAINED EARNINGS AS OF JUNE 30, 2002

Operating Revenues	
Foundation Payments	$ 2,546,830
Disadvantaged Pupil Impact Aid	20,223
State Special Education	721,349
Other Operating Revenue	25,334
Total Operating Revenues	3,313,736
Operating Expenses	
Salaries	1,533,104
Fringe Benefits	419,480
Purchased Services	868,873
Materials and Supplies	188,882
Depreciation	114,088
Other Operating Expenses	181,532
Total Operating Expenses	3,305,959
Operating Income	7,777
Non-Operating Revenues/Expenses	
Interest Income	33
Interest Expense	(12,568)
Federal Grants	19,983
State Grants	155,000
Loss on Fixed Assets (See Note 5)	(22,846)
Total Non-Operating Revenues/Expenses	139,602
Net Income	147,379
Accumulated Deficit at Beginning of Year Restated -- See Note 18	(43,655)
Retained Earnings at End of Year	$ 103,724

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

HARMONY COMMUNITY-CINCINNATI, INC.
HAMILTON COUNTY

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2002

Increase (Decrease) in Cash	
Cash Flows from Operating Activities	
Cash Received from State of Ohio	$ 3,462,315
Cash Payments to Employees for Services and their benefits	(2,148,484)
Cash Payments to Suppliers for Goods and Services	(1,176,646)
Cash Prepayments to Vendors	(67,962)
Other Operating Revenue	25,334
Net Cash Provided by Operating Activities	94,557
Cash Flows from Noncapital Financing Activities	
State and Federal Grants Received	174,983
Net Cash Provided by Noncapital Financing Activities	174,983
Cash Flows from Capital and Related Financing Activities	
Acquisition of Capital Assets	(44,774)
Capital Lease Payable Payments	(4,020)
Increase in Security Deposits	(127,045)
Short Term Loan Payments	(39,448)
Short Term Loan Proceeds	45,397
Line of Credit Proceeds	91,910
Net Cash Used for Capital and Related Financing Activities	(77,980)
Cash Flows from Investing Activities	
Cash used for Interest Expense	(12,568)
Cash Received from Interest Revenue	33
Net Cash Provided from Investing Activities	(12,535)
Net Increase in Cash	179,025
Cash at Beginning of Year	25,153
Cash at End of Year	$ 204,178
Reconciliation of Operating Income to Net Cash Provided by Operating Activities	
Operating Income	$ 7,777
Adjustments to Reconciled Operating Income to Net Cash Provided by Operating Activities	
Depreciation	114,088
Changes in Assets and Liabilities	
Decrease in Intergovernmental Receivable	173,913
(Increase) in Prepaid Items	(67,962)
(Decrease) in Accounts Payable	(11,359)
Increase in Accrued Payables	74,000
(Decrease) in Intergovernmental Payable	(45,272)
(Decrease) in Accrued Wages	(150,628)
Total Adjustments	86,780
Net Cash Provided by Operating Activities	$ 94,577

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

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NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2002

1. DESCRIPTION OF THE SCHOOL AND REPORTING ENTITY

Harmony Community – Cincinnati, Inc., Hamilton County, Ohio (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 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, the sponsor, on June 9, 1998 for a three year contract. The State Board of Education approved the proposal and entered into a contract with the Management Cabinet of the School. By-Laws of the School 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. During the fiscal year ended 2002, a contract extension for two years was executed.

The fiscal operations of the School are under a seven-member Management Cabinet, which is directed by the Executive Director. This Cabinet is responsible for formulating policies regarding fiscal operations and monitoring the expenditure of funds. The Chief Financial Officer of the School directs the financial affairs of the School including accounting, and insurance and is responsible for reporting the progress of the School against those responsibilities.

Currently, one member of the Management Cabinet is the spouse of the Executive Director and two others are full-time employees of the school.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the School have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to government nonprofit organizations. The Governmental Accounting Standards Board (GASB) is 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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

B. Measurement Focus and Basics of Accounting

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.

Revenues are recognized when they are earned. 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

All monies received by the School are accounted for by the School's Chief Financial Officer. All cash received by the Chief Financial Officer is held in an interest bearing central bank account. Total cash for the School is presented as "cash" and "cash on hand" on the accompanying balance sheet.

The School had no investments during the fiscal year.

E. Capital Assets and Depreciation

Capital assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated capital assets are recorded at their fair market value as of the dates received. The School maintains a capitalization threshold of five 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, computer software, and textbooks is computed using the straight-line method over an estimated useful life of five years. Improvements to capital assets are depreciated over the remaining useful lives of the related capital assets.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

F. Intergovernmental Revenues

The School currently participates in the State Foundation Program, State Special Education Program and the State Disadvantaged Pupil Impact Aid (DPIA) Program. 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.

The Academy also participates in other various Federal and/or State Programs through the Ohio Department of Education. Revenue received from these programs is recognized as non-operating revenue in the accounting period in which all eligibility requirements have been met.

Amounts awarded under the above named programs for the 2002 school year totaled $3,463,385.

3. CASH

At June 30, 2002, the school had a cash balance of $203,975 and cash on hand of $203 which is presented as cash and cash on hand in the accompanying financial statements. The bank balance of the School's deposits was $235,909 of which $100,000 was insured by the Federal Depository Insurance Corporation (FDIC) and the balance was insured by pooled collateral.

4. RECEIVABLES

The School had no intergovernmental receivables at June 30, 2002.

5. CAPITAL ASSETS

A summary of the School's capital assets at June 30, 2002:

Computer Hardware	$199,735
Computer Software	91,992
Furniture & Equipment	96,429
Textbooks	154,585
Total Fixed Assets	$542,742
Less: Accumulated Depreciation	(351,212)
Net Fixed Assets	$191,530

5. CAPITAL ASSETS (Continued)

The School had $22,846 (net of accumulated depreciation) in leasehold improvements, which were abandoned in June 2002.

6. 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 2002, the School contracted with Indiana Insurance Companies for property and general liability insurance. There is a $1,000 deductible with a one hundred percent blanket, all risk policy.

There were no significant reductions in insurance coverage from the prior year. Also, there were no settlements that exceeded insurance coverage for the past three years.

B. Workers Compensation

The School pays the State Workers 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.

7. CAPITAL LEASE

The School leases a copier for $1,089 a month with an imputed interest rate of 6.25% for five years. The lease qualifies as a capital lease and is recorded as a fixed asset at the present value of the future minimum lease payments. The copier is depreciated by the School over the term of the lease and the capitalized value of the copier is $16,350.

The future minimum lease payments are as follows:

Year Ended June 30	
2003	13,068
2004	5,462
Total minimum lease payments	18,530
Less: imputed interest	(6,437)
Present value of net minimum lease payments	$12,093

Insurance of the copier is the responsibility of the School.

8. DEFINED BENEFIT PENSION PLAN

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. Chapter 3309 of the Ohio Revised Code establishes benefits. SERS issues a publicly available financial report that includes financial statements and required statements and required supplementary information for SERS. This 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 at an actuarially determined rate. The current rate is 14 percent of annual covered payroll for fiscal year 2002; 5.46 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 adequacy of the contribution rates is determined annually. The School's required contribution for pension obligations to SERS for the fiscal years ended June 30, 2002, 2001, and 2000 were $44,365, $73,957 and $28,841 respectively; 57 percent has been contributed for fiscal year 2002 and 100 percent for fiscal year 2001 and 2000. $33,719 represents the unpaid contributions for fiscal year 2002 and is recorded as a liability. As of August 18, 2003, the School had met its obligation with deductions from their school foundation receipts.

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. Chapter 3307 of the Ohio Revised Code establishes benefits. STRS issues a publicly available financial report that includes financial statements and required supplementary information for STRS. This report may be obtained by writing to the State Teachers Retirement System, 275 East Broad Street, Columbus, Ohio 43215-3771.

Plan members are required to contribute 9.3 percent of their annual covered salary and the Academy is required to contribute 14 percent; 9.5 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 obligations to STRS for the fiscal years ended June 30, 2002, 2001, and 2000 were $66,453, $62,446 and $40,073 respectively; 100 percent has been contributed for all fiscal years.

9. POST EMPLOYMENT 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.

All STRS benefit recipients and sponsored dependents are eligible for health care coverage. The STRS Board has statutory authority over how, if any, of the health care costs will be absorbed by STRS. Most benefit recipients pay a portion of the health care cost in the form of a monthly premium. By Ohio Law, the cost of coverage paid from STRS funds is included in the employer contribution rate, currently 14 percent of covered payroll. The STRS board currently allocates employer contributions equal to 4.5 percent of covered payroll to the Health Care Reserve Fund. For the School, this amount equaled $32,425 during the 2002 fiscal year.

STRS pays health care benefits from the Health Care Reserve Fund. At June 30, 2001 (the latest information available) net health care costs paid by STRS were $300,772,000 and STRS had 102,132 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 8.54 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, prorated for partial service credit. For fiscal year 2002, the minimum pay has been established at $12,400. For the School, the amount to fund health care benefits, including surcharge, equaled $69,392 during the 2002 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 150 percent of annual health care expenses. Expenses for health care at June 30, 2001 (the latest information available), were $161,439,934 and the target level was $242.2 million. At June 30, 2001, SERS had net assets available for payment of health care benefits of $315.7 million. SERS has approximately 50,000 participants currently receiving health care benefits.

10. OTHER EMPLOYEE BENEFITS

A. Insurance Benefits

The School District provides life, short-term and long-term disability insurance to all employees through a private carrier. Coverage is provided for all certified and non-certified employees.

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.

11. DEBT

During fiscal year 2002, the Treasurer entered into a line of credit with Provident Bank with a limit of $150,000 at an interest rate of 6.75 percent. As of June 30, 2002, $201,910 was borrowed against the limit. Principal and interest are immediately due and payable on demand. Monthly payments shall be equal to accrued and unpaid financial charges and are to be paid each month until the principal is paid. The line of credit is collateralized by the School's inventory, chattel paper, accounts, equipment and general intangibles, assignment of warrant payment from the State of Ohio.

Debt	Balance as of 07/01/01	Increases	Decreases	Balance as of 06/30/02
Capital Lease	$16,113	0	4,020	12,093
Short-Term Loan	0	45,397	39,448	5,949
Line of Credit	110,000	91,910	0	201,910
Total	$126,113	$137,307	$ 43,468	$219,952

The line of credit is evidenced by a promissory note. Notes are statutorily limited to maturing at the end of the year unless the debt issued obligates or is collateralized by the State monies received by the School under Ohio Law. The line of credit above issued during the year does not specifically exclude State foundation monies and extended beyond year-end, contrary to State statutes. The Line of Credit balance as of August 31, 2003 was approximately $133,000 which is scheduled to be paid in full in April 2004.

12. 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 over the case and directed "…the Ohio General Assembly to enact a school-funding scheme that is thorough an efficient…" The School District is currently unable to determine what effect, if any, this decision will have on its future State funding and its operations.

13. RELATED PARTIES

During fiscal year 2002, 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 as a guidance counselor. Salaries for the Director and his wife were $79,500 and $39,273, respectively. Another Cabinet member is employed by the School as a part-time teacher. The salary of the employee is $10,400.

14. PURCHASED SERVICES

Purchased Services during fiscal year 2002 were comprised of the following:

Utilities	$53,793
Insurance	19,054
Student Development/Testing	72,671
Professional Fees	286,391
Building Lease	332,775
Security	14,455
Transportation	89,734
Total	$868,873

15. 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 is subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the School. 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, 2002.

B. Litigation

Franklin County Common Pleas Court: 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 is set for oral argument on November 18, 2003.

16. SUBSEQUENT EVENTS

The School purchased the Jewish Community Center in September 2002 to serve as a permanent home for the school. The purchase included a down payment of $150,000, and two separate long-term loans of $2,000,000 from Park National Bank and $700,000 from the Jewish Federation. At August 31, 2003, the date of the last interim statements, the outstanding amounts were $1,796,272 and $624,171 respectively.

17. MANAGEMENT'S PLAN REGARDING WORKING CAPITAL DEFICIENCY

School Management plans to pursue additional funding from the State of Ohio as follows:

The School filed an equity complaint against the State of Ohio for $475,000 alleging the state funding formula results in a disincentive to identify special education students. The lawsuit was withdrawn during the fiscal year ended June 30, 2002 pending the outcome of a federal complaint filed against the State of Ohio regarding this issue.

In 2000, ODE determined that the School was over-paid $174,660 for foundation revenue, and deducted the overpayment from the School's fiscal year 2000 foundation revenue. In December 2000, the School filed suit against ODE, asserting that ODE improperly conducted this review because there is no statutory basis for such a review.

As of August 31, 2003, the school is current on all payments required under the loans described in Notes 11 and 16, and has an unaudited cash bank balance of $96,428.

18. PRIOR PERIOD ADJUSTMENT

The Ohio Department of Education (ODE) conducted an "enrollment review" of the student full-time equivalency attendance for the fiscal year ended June 30, 1999. The ODE determined that the School was over-paid $174,660 for foundation revenue, and deducted the overpayment from the School's fiscal year 2000 foundation revenue. In December 2000, the School filed suit against ODE, asserting that ODE improperly conducted this review because there is no statutory basis for such a review. The School recorded $174,660 as Intergovernmental Receivable and Intergovernmental Revenue on the financial statements for the year ended June 30, 2001; however, the recognition of revenue of this disputed receivable does not conform with accounting principles generally accepted in the United States of America. Intergovernmental revenue, intergovernmental receivable, and retained earnings for the year ended June 30, 2001 were overstated by $174,660.

Therefore, the School's July 1, 2001 retained earnings has been restated as follows:

July 1, 2001 Retained Earnings	$131,005
Correction to retained earnings for revenue recognized in 2001 not in accordance with GAAP	(174,660)
Restated July 1, 2001 Retained Earnings	($ 43,655)

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

Harmony Community - Cincinnati, Inc.
Hamilton County
1580 Summit Road
Cincinnati, Ohio 45237

To the Management Cabinet:

We have audited the financial statements of Harmony Community - Cincinnati, Inc., Hamilton County, Ohio (the School), as of and for the year ended June 30, 2002, and have issued our report thereon dated September 12, 2003, wherein Note 17 we noted that the District is experiencing certain financial difficulties. 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 instances of noncompliance that are required to be reported under Government Auditing Standards which are described in the accompanying schedule of findings as items 2002-001 to 2002-005. We also noted certain immaterial instances of noncompliance that we have reported to management of the School in a separate letter dated September 12, 2003.

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 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 the School's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. The reportable conditions are described in the accompanying schedule of findings as items 2002-006 through 2002-008.

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 items 2002-006 and 2002-008 to be material weaknesses. 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 management of School in a separate letter dated September 12, 2003.

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.

Betty Montgomery

Betty Montgomery
Auditor of State

September 12, 2003

SCHEDULE OF FINDINGS
FOR THE YEAR ENDED JUNE 30, 2002

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

FINDING NUMBER 2002-001

Finding for Recovery

State ex rel. McClure v. Hagerman, 155 Ohio St. 320 (1951), provides that expenditures made by a public entity serve a proper public purpose. *McClure* indicates that as a general rule, the question of whether the performance of an act or the accomplishment of a specific purpose constitutes a "public purpose" for which funds may be lawfully disbursed rests in the judgment of the authorities, unless arbitrary or unreasonable.

In fiscal year 2002, the School maintained a Visa credit card through Provident Bank. Authorized users of this credit card included David Nordyke (Director), Floyd Moore (Head of Maintenance) and Dan Mooney (Principal). The school policy required these individuals to submit all receipts to the Treasurer before the school paid the credit card charges.

Four Visa invoices paid during fiscal year 2002 included receipts and documentation from only Mr. Moore and Mr. Nordyke. Any documentation needed to substantiate the purchases made by Mr. Mooney as serving a proper public purpose was unavailable.

The above reasons led to the following finding for recovery from Dan Mooney. Listed here are the unsubstantiated amounts charged by Mr. Mooney:

Visa statement, dated 2/11/02, paid with check # 4888.	$543.00
Visa statement, dated 3/11/02, paid with check # 5083.	1,355.92
Visa statement, dated 4/10/02, paid with check # 5211.	1,543.86
Visa statement, dated 5/10/02, paid with check # 5210.	1,374.90
	$4,654.03

All employees are bonded with Hamilton Mutual.

In accordance with the foregoing facts, and pursuant to Ohio Rev. Code, Section 117.28, a Finding for Recovery in favor of Harmony Community-Cincinnati, Inc. in the amount of $4,654.03, for the illegal expenditure of public monies, is hereby issued against Dan Mooney, Robert Witt, Treasurer, and Hamilton Mutual, jointly and severally.

FINDING NUMBER 2002-002

Material Noncompliance

Ohio Rev. Code, Section 3314.08(J), states that 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 is 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 Line of Credit with Provident Bank, evidenced by a promissory note maturing on May 20, 2002. However, repayment of the loan was not made on this date and the loan had an ending balance of $201,910.38 at 06/30/02. We recommend the School repay its debt at maturity date to comply with the Ohio Rev. Code.

FINDING NUMBER 2002-003

Material Noncompliance

Ohio Rev. Code, Section 3314.10(A), states in part that employment with a community school is subject to either Ohio Revised Code, Chapter 3307 or 3309. Ohio Rev. Code, Section 3309.47, states that each school employees retirement system contributor shall contribute eight per cent of the contributor's compensation to the employee's savings fund. Ohio Rev. Code Section 3309.49 requires each employer to pay to the school employees' retirement system an amount certified by the secretary that shall be a certain percent of the earnable compensation of SERS payments throughout the year. When timely payments are not made the school could incur unnecessary penalty fees, and employees may not receive appropriate retirement benefits. At June 30, 2002, the School owed $33,719 in employer and employee portions to SERS for fiscal year 2002 payroll. We recommend Management monitor payment deadlines and ascertain payments to SERS are paid by the due date.

FINDING NUMBER 2002-004

Material Noncompliance

Harmony Charter agreement between the school and Ohio Dept. of Education, Section 7, states that the following procedures must be in place to provide proper control over non-payroll disbursements:

- All expense request forms submitted as part of the Harmony Board approved budget must be approved by the School Director. A complete expenditure form is approved by the director.
- When the property is received or services performed, a receiving report is prepared, matched with the completed expenditure request form, and forwarded to bookkeeping for processing.
- Invoices and supporting documentation are stamped "Paid" upon payment.

During our test of non-payroll cash disbursements, we noted that 92% of expense request forms were not signed as evidence of the School Director's approval. Also, there were no receiving reports completed or evidence that these items were marked or stamped as "Paid." Not performing these controls is in noncompliance with the ODE contract and increases the risk of assets being misappropriated. We recommend that all expense request forms be approved and signed by the Director and that there only be two authorized signatories on all bank accounts. Once the goods are received or services rendered, a receiving report should be completed and attached to the invoice and expense request form. The three documents should be compared for accuracy, a check written, and the invoice marked as paid. The expense request form, receiving report and vendor invoice should be maintained and filed together.

FINDING NUMBER 2002-005

Material Noncompliance

Harmony Charter agreement between the school and Ohio Dept. of Education, Section 7, states that the following procedures must be applied by the school to help establish a favorable control environment and to aid in identifying misstatements either as they occur or through the review process:

- Approval in advance by the Management Cabinet to hire all employees of the School;
- Approval should be made by the Management Cabinet for all pay rates;
- All employees' timesheets should be approved by their supervisor;
- The Director should review the pay report each pay period.

FINDING NUMBER 2002-005
(Continued)

- The Director (or his designee) should distribute the paychecks and each employee should sign a form saying that he/she received it.

The following instances of noncompliance with the school contract with the Ohio Department of Education were noted in the system for processing payroll:

- Ninety percent of the employees hired and eighty percent of the employees terminated were not approved by the Management Cabinet, nor was the established rate for the positions approved.

- Five percent of time cards tested were not approved by the employee's supervisor.

- Individual pay reports were not reviewed or approved by the Director.

- Employee checks were not distributed by the Director and signed for by the individual employees.

These discrepancies could result in an overpayment, or unauthorized payment relating to payroll expenditures to occur because employees could be paid for time they are not authorized to work.

FINDING NUMBER 2002-006

Material Weakness

Monitoring Controls

An effective monitoring control system has not been implemented to assist management in detecting material misstatements in financial or other information. The School should develop and implement a monitoring control system to reduce the risk of not detecting material misstatements.

Monitoring controls are comprised of regular management and supervisory activities established to oversee whether management's objectives are being achieved. These controls should address operational, legal compliance, and financial control objectives. Effective monitoring controls should identify unexpected results or exceptions (including significant compliance exceptions), investigate underlying causes, and take corrective action. There was no documentation in the minutes that the Board reviews financial information on a regular basis.

Monitoring controls may be in the nature of ongoing activities or separate periodic evaluation by either management or an internal audit function. They can relate to a specific transaction cycle or can be more overview in nature.

Monitoring controls should assist management in detecting material misstatements in financial or other information and can include:

- regular review of budget and actual expenditures by the Management Cabinet;

- regular review of financial report summaries of sufficient detail (monthly detailed revenue and expenditure reports), review of monthly reconciliations and approval by the Management Cabinet in the minutes;

- review of key performance indicators by the Management Cabinet;

- review of revenues/expenditures with independently accumulated information (budgets, past performance, etc.) by the Management Cabinet;

FINDING NUMBER 2002-006
(Continued)

- review of unusual or significant items, long outstanding items, and identification of unusual fluctuations – etc. by the Treasurer;

- the Management Cabinet should ensure that adequate segregation of duties exist;

- approval of grants by the Director;

- Monthly reports, including general ledger, bank reconciliations and payroll, are prepared and reviewed by Management Cabinet at every meeting.

FINDING NUMBER 2002-007

Reportable Condition

The School does not have an employee reimbursement policy which requires employees to submit receipts for reimbursement. The School advances money to employees (with the Director's approval) who are attending a seminar to cover their travel costs. Without proper documentation and/or receipts to support travel costs, reimbursements to School employees could result in a Finding for Recovery for illegal expenditures that are not a proper public purpose.

The School should establish a policy and procedures regarding employee reimbursements. This policy should include requiring receipts for all purchases made, completion of reimbursement forms with the employee's signature indicating the items for which the employee is being reimbursed are for a proper public purpose, and approval from management authorizing the reimbursement.

FINDING NUMBER 2002-008

Material Weakness

The School does not have a fixed asset policy or a formal system of tracking, tagging and valuing fixed assets. We recommend the School adopt a fixed asset tracking and valuation system. This system should provide supporting documentation on each fixed asset. Such information should include, but not be limited to, date of purchase or acquisition, brief description of the asset; location of asset; identification number; purchase price; estimated useful life; disposition date, and amount received on disposition. The system should categorize assets by major type (e.g., land, buildings, equipment) and should summarize the amount invested in fixed assets by major type. The system should also record and summarize depreciation expense and accumulated depreciation for each fixed asset. The system should provide for perpetual updating of this information.

The lack of a fixed asset system and established procedures to monitor additions and deletions will decrease the School's ability to safeguard its fixed assets. Establishing a fixed asset system and policies and procedures will improve control over School property by decreasing the risk of loss and misappropriation. Perpetual maintenance of such information will also assist the School in maintaining adequate insurance coverage, as well as provide support evidence in case of theft or fire losses.

HARMONY COMMUNITY - CINCINNATI, INC.
HAMILTON COUNTY

SCHEDULE OF PRIOR AUDIT FINDINGS
JUNE 30, 2002

Finding Number	Finding Summary	Fully Corrected?	Not Corrected, Partially Corrected; Significantly Different Corrective Action Taken; or Finding No Longer Valid; ***Explain***:
2001-10431-001	Finding for Recovery.	No	No action taken
2001-10431-002	Material Noncompliance: Debt issue extended beyond fiscal year	No	Reissued as Finding 2002-002.
2001-10431-003	Material Noncompliance & Reportable Condition: School not current on its payments to SERS.	No	Reissued as Finding 2002-003.
2001-10431-004	Reportable Condition: Failure to file with IRS	Yes	
2001-10431-005	Material Weakness: Lack of monitoring controls by management	No	Reissued as Finding 2002-006.
2001-10431-006	Material Weakness: No reimbursement policy	No	Reissued as Finding 2002-007.

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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
OCTOBER 16, 2003