NEW CHOICES COMMUNITY SCHOOL
MONTGOMERY COUNTY

REGULAR AUDIT

FOR THE YEAR ENDED JUNE 30, 2003

Auditor of State
Betty Montgomery

NEW CHOICES COMMUNITY SCHOOL
MONTGOMERY COUNTY

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Auditor of State
Betty Montgomery

INDEPENDENT ACCOUNTANTS' REPORT

New Choices Community School
Montgomery County
601 S. Keowee Street
Dayton, Ohio 45410

To the Board of Governance:

We were engaged to audit the accompanying Balance Sheet of New Choices Community School, Montgomery County, (the School), as of and for the year ended June 30, 2003, and the related Statement of Revenues, Expenses, and Changes in Retained Earnings/Accumulated Deficit and Statement of Cash Flows for the year then ended. These financial statements are the responsibility of the School's management.

We were unable to obtain sufficient evidential matter to support Cash and Accounts Payable, nor were we able to satisfy ourselves as to those financial activities by other auditing procedures.

Because of the lack of sufficient competent evidential matter, and we were unable to apply other auditing procedures regarding cash and accounts payable as discussed in the preceding paragraph, the scope of our work was not sufficient to enable us to express, and we do not express, an opinion on the financial statement referred to in paragraph 1.

As indicated in the financial statements, for the year ended June 30, 2003, the School incurred a net loss of $488,568, a working capital deficiency of $510,809, and a accumulated deficit retained earnings of $434,365. Management's plans to eliminate the deficit is discussed in Note 15.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 5, 2004, on our consideration of the School's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our engagement.

Betty Montgomery

Betty Montgomery
Auditor of State

October 5, 2004

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NEW CHOICES COMMUNITY SCHOOL
MONTGOMERY COUNTY

BALANCE SHEET
AS OF JUNE 30, 2003

Assets	
Current Assets	
Cash and Cash Equivalents with Fiscal Agent	$54,267
Intergovernmental Receivables	165,046
Total Current Assets	219,313
Non-Current Assets	
Fixed Assets (Net of Accumulated Depreciation)	76,444
Total Assets	295,757
Liabilities and Fund Equity	
Current Liabilities	
Accounts Payable	686,869
Intergovernmental Payable	28,253
Compensated Absences Payable	15,000
Total Liabilities	730,122
Fund Equity	
Accumulated Deficit	(434,365)
Total Liabilities and Fund Equity	$295,757

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

NEW CHOICES COMMUNITY SCHOOL
MONTGOMERY COUNTY

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

Operating Revenues	
Foundation Payments	$358,609
Disadvantaged Public Impact Aid	9,982
Special Education Weighted Funding	43,400
Total Operating Revenues	411,991
Operating Expenses	
Salaries	453,411
Fringe Benefits	141,601
Purchased Services	304,182
Materials and Supplies	22,115
Depreciation	20,292
Capital Outlay	144,633
Other Operating Expenses	32,049
Total Operating Expenses	1,118,283
Operating (Loss)	(706,292)
Non-Operating Revenues	
Federal Grants	185,859
State Grants	4,595
Private Grants	25,375
Miscellaneous Grants	1,895
Total Non-Operating Revenues	217,724
Net (Loss)	(488,568)
Retained Earnings at Beginning of Year	54,203
Accumulated Deficit at End of Year	($434,365)

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

NEW CHOICES COMMUNITY SCHOOL
MONTGOMERY COUNTY

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

Increase (Decrease) in Cash and Cash Equivalents	
Cash Flows from Operating Activities	
Cash received from State of Ohio	$365,455
Cash Payments to Suppliers for Goods and Services	(496,641)
Cash Payments to Employees for Services and Benefits	(586,298)
Cash Provided by Eastway Corporation	589,737
Net Cash (Used for) Operating Activities	(127,747)
Cash Flows from Noncapital Financing Activities	
State and Federal Grants Received	228,609
Private and Miscellaneous Grants	27,270
Net Cash Provided by Noncapital Financing Activities	255,879
Cash Flows from Capital and Related Financing Activities	
Payments for Capital Acquisitions	(77,846)
Net Increase in Cash and Cash Equivalents	50,286
Cash and Cash Equivalents at Beginning of Year	3,981
Cash and Cash Equivalents at End of Year	54,267
Reconciliation of Operating (Loss) to Net Cash Used for Operating Activities	
Operating (Loss)	(706,292)
Adjustments to Reconcile Operating (Loss) to Net Cash (Used for) Operating Activities	
Depreciation	20,292
Changes in Assets and Liabilities:	
Decrease in Intergovernmental Receivables	35,406
Increase in Accounts Payable	518,925
Increase in Compensated Absences Payable	1,685
Increase in Intergovernmental Payable	2,237
Total Adjustments	578,545
Net Cash (Used for) Operating Activities	($127,747)

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

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1. DESCRIPTION OF THE ENTITY

New Choices Community School (the School) is a nonprofit corporation established pursuant to Ohio Rev. Code Chapters 3314 and 1702 to maintain and provide a school that promotes excellence in education, character development and mental health wellness for at-risk youth in Montgomery County Ohio. The School, which is part of the State's education program, is independent of any school district and is nonsectarian in its programs, admission policies, employment practices, and all other operations. The School may sue and be sued, acquire facilities as needed, and contract for any services necessary for the operation of the school. The School qualified as an exempt organization under Section 501(c) (3) of the Internal Revenue Code.

The School was approved for operation under contract with the Ohio State Board of Education (the Sponsor) for a period of five years commencing July 30, 2001. The Sponsor is responsible for evaluating the performance of the School and has the authority to deny renewal of the contract at its expiration or terminate the contract prior to its expiration.

The School operates under the direction of a six-member Board of Directors. The Board is responsible for carrying out the provisions of the contract that include, but are not limited to, state-mandated provisions regarding student population, curriculum, academic goals, performance standards, admission standards, and qualifications of teachers. The Board of Directors controls the School's one instructional/support facility staffed by 4 non-certified and 8 certificated teaching personnel who provide services to approximately 70 students.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of New Choices Community School 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

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

B. Measurement Focus/Basis of Accounting

The accounting and financial reporting treatment is determined by its measurement focus. With this measurement focus, all assets and all liabilities are included on the balance sheet. Operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total assets

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.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. Budgetary Process

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

D. Cash and Cash Equivalents

All cash received by the School is maintained in a demand deposit account.

E. Estimates

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

F. Fixed Assets and Depreciation

Fixed assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. 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 is computed using the straight-line method over an estimated useful life of five years.

G. 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. Revenues received from 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 all eligibility requirements have been met.

The School also participates in the Federal Charter School Grant Program through the Ohio Department of Education. Under this program, the School was awarded $150,000 in Phase II funding to offset start-up costs of the School. Additionally, the School applied for and received approval for Phase III federal grant funding totaling $150,000.

Amounts awarded under the above named programs for the 2003 school year totaled $602,445.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

H. Compensated Absences

Benefits are earned on a per pay period basis. The School records a liability for accumulated unused paid leave time when earned for all employees.

I. Accrued Liabilities

Obligations incurred but unbilled prior to June 30, 2003, are reported as accrued liabilities in the accompanying financial statements.

J. Exchange and Non Exchange Transactions

Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded on the accrual basis when the exchange takes place.

Non exchange transactions, in which the School receives value without directly giving equal value in return, include grants, entitlements and donations. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. 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.

K. Private Grants

The School received $25,175 from the Fordham Foundation. Additionally the school held various fund raising efforts rendering $1,895 in donations. Other donors contributed a combined total of $200.

3. DEPOSITS AND INVESTMENTS

At June 30, 2003, the carrying amount of the School's deposits was $54,267, which equaled the bank balance. The entire bank balance was covered by federal depository insurance.

4. INTERGOVERNMENTAL RECEIVABLES

Receivables at June 30, 2003 consisted of intergovernmental (federal grants and state foundation) receivables. All intergovernmental receivables are considered collectible in full, due to the stable condition of State programs, and the current year guarantee of federal funds. Intergovernmental receivables consisted of foundation allocation money of $48,774 and Federal School Grant funding of $116,272.

5. FIXED ASSETS

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

	Beginning Balance	Additions	Deletions	Ending Balance
Furniture and Equipment	$23,612	$77,846	-	$101,458
Less: Accumulated Depreciation	(4,722)	(20,292)	-	(25,014)
Net Fixed Assets	$18,890	$57,554	-	$76,444

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.

Professional liability is protected by Specialty National Insurance Company with a $1,000,000 single occurrence limit and $3,000,000 aggregate and no deductible. Vehicles are covered by Cincinnati Insurance Company and hold a $100 deductible for comprehensive and a $250 deductible for collision. Automobile liability has a $1,000,000 combined single limit of liability.

B. Workers' Compensation

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

7. DEFINED BENEFIT PENSION PLANS

A. School Employees Retirement System

The School contributes to the School Employees Retirement System (SERS), a cost-sharing multiple employer defined benefit pension plan. SERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by State Statue Chapter 3309 of the Ohio Revised Code. SERS issues a publicly available, stand-alone financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the School Employees Retirement System, 300 East Broad Street, Suite l00, Columbus, Ohio 43215-3476.

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 School rate is 14 percent of annual covered payroll. A portion of the School's contribution is used to fund pension obligations with the remainder being used to fund health care benefits; for fiscal year 2003, 8.17 percent of annual covered salary was the portion used to fund pension obligations. For fiscal year 2002, 5.46 percent of annual covered salary was the portion used to fund pension obligations. The contribution requirements of plan members and employers are established and may be amended, up to a statutory maximum amount, by the SERS' Retirement Board. The School's required contributions for pension obligations to SERS for the fiscal years ended June 30, 2003 and 2002 were $7,965 and $3,231 respectively; 50.54 percent has been contributed for fiscal year 2003 and 100 percent for fiscal year 2002.

7. DEFINED BENEFIT PENSION PLANS (Continued)

B. State Teachers Retirement System

The School participates in the State Teachers Retirement System of Ohio (STRS Ohio), a cost-sharing, multiple-employer public employee retirement system. STRS Ohio provides retirement and disability benefits to members and death and survivor benefits to beneficiaries. STRS Ohio issues a stand-alone financial report that may be obtained by writing to STRS Ohio, 275 E. Broad St., Columbus, OH 43215-3371 or by calling (614) 227-4090.

New members have a choice of three retirement plans, a Defined Benefit (DB) Plan, a Defined Contribution (DC) Plan and a Combined Plan. The DB plan offers an annual retirement allowance based on final average salary times a percentage that varies based on years of service, or an allowance based on member contributions and earned interest matched by STRS Ohio funds times an actuarially determined annuity factor. The DC Plan allows members to place all their member contributions and employer contributions equal to 10.5% of earned compensation into an investment account. Investment decisions are made by the member. A member is eligible to receive a retirement benefit at age 50 and termination of employment. The Combined Plan offers features of both the DC Plan and the DB Plan. In the Combined Plan, member contributions are invested by the member, and employer contributions are used to fund the defined benefit payment at a reduced level from the regular DB Plan. DC and Combined Plan members will transfer to the Defined Benefit Plan during their fifth year of membership unless they permanently select the DC or Combined Plan. Existing members with less than five years of service credit as of June 30, 2001, were given the option of making a one time irrevocable decision to transfer their account balances from the existing DB Plan into the DC Plan or the Combined Plan. This option expired on December 31, 2001. Benefits are established by Chapter 3307 of the Ohio Revised Code.

A DB or Combined Plan member with five or more years credited service who becomes disabled may qualify for a disability benefit. Eligible spouses and dependents of these active members who die before retirement may qualify for survivor benefits. Members in the DC Plan who become disabled are entitled only to their account balance. If a member dies before retirement benefits begin, the member's designated beneficiary is entitled to receive the member's account balance

For the fiscal year ended June 30,2003, plan members were required to contribute 9.3 percent of their annual covered salaries. The School was required to contribute 14 percent; 13 percent was the portion used to fund pension obligations. For fiscal year 2002, the portion used to fund pension obligations was 9.5 percent. Contribution rates are established by the State Teachers Retirement Board, upon recommendations of its consulting actuary, not to exceed statutory maximum rates of 10% for members and 14% for employers. Chapter 3307 of the Ohio Revised Code provides statutory authority for member and employer contributions.

The School's required contributions for pension obligations for the fiscal years ended June 30, 2003 and 2002 were $60,118 and $23,808 respectively; 81.69 percent has been contributed for fiscal year 2003 and 100 percent for fiscal years 2002.

8. POSTEMPLOYMENT BENEFITS

State Teachers Retirement System of Ohio (STRS Ohio) provides comprehensive healthcare benefits to retirees and their dependents. Coverage includes hospitalization, physicians' fees, prescription drugs, and partial reimbursement of monthly Medicare premiums. All benefit recipients and sponsored dependents are eligible for health care coverage. Pursuant to the Ohio Revised Code (R.C.), the State Teachers Retirement Board (the Board) has discretionary authority over how much, if any, of the health care costs will be absorbed by STRS Ohio. Most benefit recipients pay a portion of the health care cost in the form of a monthly premium. The R.C. grants authority to STRS Ohio to provide health care coverage to benefit recipients, spouses and dependents. 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 Retirement Board allocates employer contributions to the Health Care Stabilization Fund from which health care benefits are paid. For fiscal year ended June 30, 2003, the Board allocated employer contributions equal to 1.0 percent of covered payroll to the Health Care Stabilization Fund. For fiscal year ended June 30, 2002, 4.5% of covered payroll was allocated to the fund. The balance in the Health Care Stabilization Fund was $2.8 billion on June 30, 2003. For the School, this amount equaled $4,624 during the 2003 fiscal year.

For the year ended June 30, 2003, net health care costs paid by STRS Ohio were $352,301,000. There were 108,294 eligible benefit recipients.

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

After the allocation for basic benefits, the remainder of the employer's 14 percent contribution is allocated to providing health care benefits. For the fiscal year ended June 30, 2003, the allocation rate is 5.83 percent. In addition, SERS levies a surcharge to fund health care benefits equal to 14 percent of the difference between a minimum pay and the member's pay, pro-rated for partial service credit. For fiscal year 2003, the minimum pay has been established at $14,500. For the School, the amount to fund health care benefits, including the surcharge, was $5,683 for fiscal year 2003.

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, 2003, were $204,930,737 and the target level was $307.4 million. At June 30, 2003, the Retirement System's net assets available for payment of health care benefits of $303.6 million. The number of benefit recipients currently receiving heath care benefits is approximately 50,000.

9. CONTINGENCIES

A. Grants

The School received financial assistance from federal and state agencies in the form of grants. The disbursement of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and are subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the general fund or other applicable funds. Such disallowed claims would have a material adverse effect on the overall financial position of the School at June 30, 2003.

B. State Funding

The Ohio Department of Education conducts reviews of enrollment data and full-time equivalency calculations made by the schools. These reviews are conducted to ensure the schools are reporting accurate student enrollment data to the State, upon which state foundation funding is calculated. The conclusion of this review has resulted in state funding being adjusted for fiscal year 2004. The fiscal year 2003 adjustment to state funding for the School is a reduction in the amount of $14,885, for fiscal year 2004. This amount is included in the financial statements as intergovernmental payable.

C. Litigation

A suit was filed in Franklin County Common Pleas Court on May 14, 2001 alleging that Ohio's Community (i.e., Charter) Schools program violates the state Constitution and state laws. On April 21, 2003, the court dismissed the counts containing constitutional claims and stayed the other counts pending appeal of the constitutional issues. The plaintiffs appealed to the Court of Appeals, the issues have been briefed, and the case was heard on November 18, 2003. On August 24, 2004, the Court of Appeals rendered a decision that Community Schools are part of the state public educational system and this matter was sent to the Ohio Supreme Court. The effect of this suit, if any, on the New Choices Community School is no presently determinable.

D. State Contract

The School received approximately 100 percent of its operating income from the State of Ohio. Accordingly, the risk exists that the ability to continue the contract with the state of Ohio could affect the financial status of the School.

10. MANAGEMENT SERVICES CONTRACT

The School entered into a one-year contract on July 1, 2002, with Eastway Corporation for management services. Under the contract, Eastway is required to provide core management services including accounting and reporting, financial, payroll, budgeting, quality assurance, program evaluation, information systems management, clinical information system management, recruitment and hiring, personnel management, employee relations and employee benefit management. Eastway receives a management fee equal to 10% of the School’s total expenses for these services. For the year ended June 30, 2003, the School expensed $99,996 under this contract. One School Board member is also Chief Executive Officer of Eastway Corporation.

Expenses incurred by the School but paid by Eastway Corporation have been reported as Accounts Payable on the Schools financial statements. Contrary to Ohio law, the School’s management company failed to provide a detailed accounting including the nature and cost of the services it provided to the School. Further, this information was not included in the footnotes of the financial statements of the School.

11. PURCHASED SERVICES

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

Management Company Expenses	$99,996
Occupancy Costs	60,053
Travel	7,296
Advertising and Promotion	16,477
Food Service	51,345
Trade Services	51,320
Utilities	17,695
	$304,182

12. STATE SCHOOL FUNDING

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

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

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

13. OPERATING LEASES

The School leases its facilities from the Dayton Boys and Girls Club under an initial lease agreement beginning September 23, 2002 and ending June 30, 2005. The monthly lease payments during fiscal year 2003 were $2,000. Total rental payments for fiscal year 2003 were $20,000 with an additional $2,000 security deposit required. Rent payments are expected to remain the same for fiscal year 2004.

14. SUBSEQUENT EVENTS

On March 2, 2004, the School’s Board of Directors adopted a resolution approving amendment to the code of regulations in the School’s charter with the Ohio Department of Education, removing Eastway Corporation as the sole member, and amending the principle office to the New Choices Community School.

On November 25, 2003, the School’s Board passed a resolution approving the “Continued Security Agreement” between New Choices Community School and Eastway Corporation. The signed agreement was needed by Eastway for a loan from Huntington Bank, part of which involves expenses Eastway incurred on behalf of the School. The agreement authorizes the School’s assets be used as collateral for the School’s share of the debt owed to Eastway.

14. SUBSEQUENT EVENTS (Continued)

On November 25, 2003, the School's Board passed a resolution approving a promissory note between the School and Eastway Corporation for an amount not to exceed $447,000, with the final amount to be determined upon further examination by the School's Treasurer. The Note was presented without a set amount due to discrepancies involving overpayment of staff salaries and questions regarding management fees.

15. MANAGEMENT'S PLANS REGARDING ACCUMULATED DEFICIT

The School has accumulated a deficit of $434,365 for the year ended June 30, 2003. The deficit is due in large part to expenditures spent on the School's behalf by the management company. Management plans to eliminate the deficit by implementing financial policies that will allow the School to operate independently of the management company.

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Auditor of State
Betty Montgomery

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

New Choices Community School
Montgomery County
601 S. Keowee Street
Dayton, Ohio 45410

To the Board of Governance:

We were engaged to audit the financial statements of New Choices Community School, Montgomery County, (the School), as of and for the year ended June 30, 2003, and have issued our report thereon dated October 5, 2004, wherein we issued a disclaimer of opinion and we noted the School has a negative working capital and a accumulated deficit.

Compliance

As part of our engagement we performed tests of compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could directly and materially affect 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 we must report under *Government Auditing Standards* which are described in the accompanying schedule of findings as items 2003-001 through 2003-004. We also noted certain immaterial instances of noncompliance that we have reported to management of the School in a separate letter dated October 5, 2004.

Internal Control Over Financial Reporting

In planning and performing our engagement, we considered the School's internal control over financial reporting 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 management's assertions in the financial statements. Reportable conditions are described in the accompanying schedule of findings as items 2003-005 through 2003-009.

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Internal Control Over Financial Reporting
(Continued)

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 2003-005 and 2003-006 to be material weaknesses. We also we 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 the School in a separate letter dated October 5, 2004.

This report is intended for the information and use of the management and the Board of Governance, 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

October 5, 2004

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

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

FINDING NUMBER 2003-001

Ohio Administration Code Section 117-6-01(B) requires each community school to employ the Uniform School Accounting System (USAS). The USAS employs a system of dimensions (codes) which serves to identify in detail each financial transaction of the School. The reporting requirements for expenditures are fund (3 digits), function (2 digits), object (1 digit) and, when required by a funding agent, special cost center (4 digits). Minimum requirements for receipts are fund (3 digits), receipt code (2 digits), and, when required by a funding agent, special cost center (4 digits). Although the School converted their transactions to USAS codes after year end, they used a system of accounting that was not in conformity with USAS during the fiscal year. This could result in inappropriate posting of revenues and expenditures, and additional effort to convert amounts to the required detail at year end.

The School should develop and implement the routine use of the Uniform School Accounting System for its daily transactions and record keeping, to reduce the potential for errors and allow for more accurate and proper presentation of financial activity.

FINDING NUMBER 2003-002

Ohio Rev. Code Section 149.43 states in pertinent part that “all public records shall be promptly prepared and made available to any member of the general public at all reasonable times during regular business hours for inspection. “Record” for purposes of the public records law, means any document, device, or item, regardless of physical form or characteristic, created, received by, or coming under the jurisdiction of any public office which serves to document the organization, functions, policies, decisions, procedures, operations, or other activities of the public office.

The School failed to maintain underlying support documentation for 18 out of 100 or 21% of expenditure transactions selected for testing. Failure to retain adequate supporting documentation could result in payment of unauthorized expenditures or overpayments.

Additionally, State Foundation Settlement Sheets were not maintained and utilized for posting state foundation revenue. As a result, state foundation revenue was not properly posted and was understated by $52,953, which was adjusted in the School’s financial statements.

The School should adopt procedures for retention of proper supporting documentation for all receipts and expenditures of public monies. Implementing these procedures will help to provide proper posting of receipts and ensure that only authorized obligations are paid.

FINDING NUMBER 2003-003

Internal Revenue Service Code Chapter 26 [26 U.S.C.] – Collection of Income Tax at Source on Wages; 26 U.S.C. 3401 through 3406 also (26 C.F.R.) 1.6041-2 and ORC 5747.06 indicate that the employees’ wages of New Choices Community School should be reported under an Employer Identification Number (EIN) assigned to New Choices Community School, in accordance with the Collection of Ohio Income Tax at source.

New Choices Community School did not file IRS forms 941 Quarterly Payroll Tax Form or form W-2 for calendar year 2002. Wages of the employees of New Choices Community School were reported as Eastway Corporation’s (management company) wages and not the School’s.

FINDING NUMBER 2003-003
(Continued)

The School did not report wages to federal agencies or the State of Ohio under the entity name and identification number of New Choices Community School. Review of the School's employees' 2002 W-2 forms, revealed the entity identification number and employer's information in boxes b and c were that of the Eastway Corporation.

The School should file all applicable federal and state forms for wages earned for the period correctly identifying wages earned as the School's expenditures under a separate EIN. This will help to provide compliance with applicable federal and state laws and help reduce the possibility of additional expenditures to the school for fines imposed for improper tax filings.

FINDING NUMBER 2003-004

Ohio Rev. Code Section 117.38 requires that GAAP-basis entities must file annual reports within 150 days of fiscal year end. These reports must be filed on forms prescribed by the Auditor of State (AOS). However, if the Auditor of State has not prescribed a form for the report, the public office shall submit its report on the form utilized by the public office. Any public office which does not file the report by the required date shall pay a penalty of twenty-five dollars for each day the report remains unfiled, not to exceed seven hundred fifty dollars. The Auditor of State may provide waivers of these dates and penalties in certain circumstances.

The School failed to file its GAAP-basis financial report for the year ended June 30, 2003, by the required date, nor was a waiver requested or extension filed with the AOS. The School should develop and implement procedures to ensure that the annual financial report is prepared and filed timely. Timely reporting will reduce the likelihood of late fines being imposed and should provide improved information for financial decision making purposes.

FINDING NUMBER 2003-005

Auditor of State Bulletin 2000-005 states the management of each community school is responsible for the design and implementation of an internal control process that provides reasonable assurance of the integrity of its financial reporting, the safeguarding of its assets, the efficiency and effectiveness of its operation, and its compliance with applicable laws, regulations, and contracts. In designing its internal control process, management should consider policies and procedures that provide for the following:

- Appropriate authorization and approval of transactions.
- Adequately design records to facilitate classification and summarization of transactions.
- Security of assets and records.
- Segregation of incompatible duties.
- Periodic reconciliations of account balances.
- Periodic verification of assets.

The School had little or no controls over cash reconciliations, recording financial transactions to the accounting ledgers, documenting cash disbursements, and record retention. Additionally, the School's management transferred monies between bank accounts without the proper authorization of the Governing Board. The School should design and implement internal control procedures that provide reasonable assurance of the integrity of its financial reporting.

FINDING NUMBER 2003-006

Monthly Bank-to-Book Reconciliations

Deficiencies were noted in the School's completion of monthly bank-to-book reconciliations. Monthly bank-to-book reconciliations should be prepared, and all accounts belonging to the School should be included on the monthly reconciliation. The following deficiencies were noted in monthly bank-to-book reconciliations which resulted in inaccurate fund balances and incorrect amounts in the appropriations and receipts ledgers:

- Monthly bank-to-book reconciliations were either not accurately prepared or not prepared at all for the entire period under audit;
- The School's cash fund balances, did not agree to the monthly bank to book reconciliations for the entire period under audit;
- There was no indication that the Board reviewed bank to book reconciliations.

Risks associated with these conditions include the possibility of loss of revenue; missing or duplicate posting of cash receipts and disbursements; and reconciliation errors that could go undetected. To strengthen internal accounting controls, reduce errors in recording transactions, and to provide management with reasonable assurance that cash reconciliation procedures are in place, the following controls should be implemented:

- Monthly bank-to-book reconciliations should be prepared.
- Interest from all accounts should be posted monthly.
- The monthly bank-to-book reconciliations should be reviewed by the Board, along with a list of outstanding checks.
- The reconciled bank balance should be compared to the cashbook balance to ensure the amounts correspond.
- The balance of the cashbook should be reviewed to ensure that all active and invested money under the control of the Board is included. The Board should date and initial the monthly reconciliation as documentation of their review.

FINDING NUMBER 2003-007

Proper Payment to Employees

During testing of gross payroll amounts, it was noted that the School overpaid five employees a total of $35,630 in gross wages, or 3% of the School's operating expenditures for fiscal year 2003. Although the School's Board of Governance passed a resolution dated August 3, 2004, approving the salary overpayments, the overall effect of the additional wage payments resulted in a reduction of funds that would have been available to fund other school activities and/or purchases.

The School should take the necessary steps needed to develop and implement control procedures that would prevent future overpayments of employees. The procedures should be approved by the School's Board and should include a periodic review and comparison of gross payroll amounts to Board approved contract rates. Implementation of additional payroll controls will reduce the likelihood of payroll overpayments, and will provide management with realistic expenditure amounts needed for future budgetary planning.

FINDING NUMBER 2003-008

Fixed Assets

The School did not develop or implement a Board approved fixed asset policy to address asset capitalization issues, or procedures to account for additions and deletions of fixed assets throughout the year. Additionally, the School did not have a fixed asset accounting system which maintains a total fixed asset listing and other supplemental information for the School's asset inventory. Further, the School did not perform periodic physical inventories of the fixed assets. Failure to obtain timely records or employ adequate controls over the acquisition and disposal of fixed assets could result in misappropriation of assets and misstatements of recorded assets on the financial statements.

To assist the School in maintaining adequate controls over their fixed assets, and reduce the risk that the School's fixed assets will be materially misstated, the Board should develop and implement appropriate fixed asset policies and procedures to be performed throughout the year for the timely maintenance of fixed asset records. At a minimum, these policies and procedures should address establishing a capitalization threshold; tagging and recording of purchased assets meeting the School's established capitalization threshold; accounting for asset additions and deletions; performance of an annual physical inventory of fixed assets and reconciliation to asset records; computing of periodic depreciation; and asset disposal procedures. Fixed asset records should include such information as a description of the item, the cost, the acquisition date, location, tag number, and any other supporting information. Reasonable estimated lives for assets should also be developed and used in the periodic depreciation of assets.

The School should also develop and maintain a fixed asset accounting system which accurately represents all fixed assets owned by the School. The system should be capable of maintaining a complete asset inventory, indicating asset tag number; location; date acquired, cost, manufacture, model and serial number, and useful life.

Implementation of a comprehensive fixed asset policy and procedure will allow the Board to use accurate information in decision making process, and give an accurate accounting for annual depreciation and maintenance expenses. Further, accurate records will increase the School's ability to secure recovery in the event of the loss of assets.

FINDING NUMBER 2003-009

GAAP Policies and Procedures

The School did not formally establish Generally Accepted Accounting Principles (GAAP) policies and procedures used for determining accrued receivables and liabilities for preparation of the basic financial statements. Additionally, the School could not provide supporting documentation for the Accounts payable line item which is 94% of total liabilities. Failure to establish GAAP policies and procedures or maintain adequate support documentation could result in the financial statements and notes not being consistent and comparable from year to year as required by accounting reporting standards.

We recommended that the School establish and implement GAAP Policies and procedures, and preserve supporting documentation for determining accrued receivables and liabilities at year end in order to ensure consistent and comparable financial reporting.

NEW CHOICES COMMUNITY SCHOOL
MONTGOMERY COUNTY

SCHEDULE OF PRIOR YEAR FINDINGS
JUNE 30, 2003

Finding Number	Finding Summary	Fully Corrected?	Not Corrected, Partially Corrected; Significantly Different Corrective Action Taken; or Finding No Longer Valid; ***Explain***:
2002-10357-001	OAC 117-6-01 (B): School failed to employ USAS for recording of revenues and expenditures.	No	Repeated in current year as Finding 2003-001
2002-10357-002	ORC 3314.03(A)(11)(g): School failed to submit an annual report of activities.	Yes	
2002-10357-003	Contract between New Choices and Ohio Department of Education: School failed to provide proof of required licenses for all teachers.	No	Partially Corrected. Required certification could not be provided for one teacher. Reported to management of the school in a separate letter.
2002-10357-004	Fixed Assets: School lacked procedures to record assets as additions and deletions; School did not have a policy for periodic inventory of assets.	No	Repeated in current year as Finding 2003-008
2002-10357-005	OMB Circular A133, Subpart C, Section 300: School failed to identify federal expenditures that could be reconciled to the programs under which they were received and disbursed.	Yes	

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NEW CHOICES COMMUNITY SCHOOL

MONTGOMERY 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
NOVEMBER 30, 2004