# CONSTELLATION SCHOOLS: MADISON COMMUNITY ELEMENTARY
# CUYAHOGA COUNTY, OHIO

## REGULAR AUDIT

## FOR THE YEAR ENDED JUNE 30, 2014

**Constellation Schools**

*"The Right Choice for Parents and a Real Chance for Children!"*

# Dave Yost · Auditor of State

Board of Trustees
Constellation Schools: Madison Community Elementary
2015 West 95th Street
Cleveland, Ohio 44102

We have reviewed the *Independent Auditor's Report* of the Constellation Schools: Madison Community Elementary, Cuyahoga County, prepared by Rea & Associates, Inc., for the audit period July 1, 2013 through June 30, 2014. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The Constellation Schools: Madison Community Elementary is responsible for compliance with these laws and regulations.

Dave Yost
Auditor of State

December 16, 2014

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**CONSTELLATION SCHOOLS: MADISON COMMUNITY ELEMENTARY**
**CUYAHOGA COUNTY, OHIO**

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# INDEPENDENT AUDITOR'S REPORT

November 25, 2014

To the Board of Trustees
Constellation Schools: Madison Community Elementary
2015 West 95th Street
Cleveland, OH 44102

## Report on the Financial Statements

We have audited the accompanying financial statements of Constellation Schools: Madison Community Elementary, Cuyahoga County, Ohio (the School), as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the School's basic financial statements as listed in the table of contents.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditor's Responsibility*

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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the School's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the School's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the School, as of June 30, 2014, and the changes in financial position, and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

***Emphasis of Matter***

As described in Note II.3 to the financial statements, during 2014, the School adopted new accounting guidance in Governmental Accounting Standards Board (GASB) Statement No. 65, *Items Previously Reported as Assets and Liabilities* and as a result restated their June 30, 2013 net position due to a reclassification of debt issuance costs as an expense in the period incurred rather than amortizing over the life of the debt. Our opinion is not modified with respect to this matter.

***Other Matters***

*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3–7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated November 25, 2014 on our consideration of the School's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the School's internal control over financial reporting and compliance.

Rea & Associates, Inc.

Medina, Ohio

The discussion and analysis of Constellation Schools: Madison Community Elementary (MDCE) financial performance provides an overall review of financial activities for the fiscal year ended June 30, 2014. The intent of this discussion and analysis is to look at the financial performance of MDCE as a whole. Readers should also review the Notes to the Financial Statements and the Financial Statements to enhance their understanding of the financial performance of MDCE.

## Financial Highlights

Key financial highlights for 2014 include the following:

- On April 10, 2014 MDCE shared in the closing of a multi-school, multi-property bond financing arrangement with the Cleveland Cuyahoga County Port Authority to refinance a prior bond issue, reacquire title to the land and buildings MDCE operates from, improve debt covenants from the prior bond issue, and complete building renovations.

- In total, net position increased $60,032, which represents a 13.0% increase from 2013. Increased State Foundation funds were partially offset by $158,879 in fees incurred to refinance a bond issue during the year, along with increases in other expenditure categories combined to create this increase.

- Total assets and deferred outflow of resources increased $333,160, which represents a 9.6% increase from 2013. This is due to cash generated from the operations of the school and increases in deferred outflows of resources and bond escrow funds offset by reductions in bond reserve accounts.

- Liabilities increased $273,128, which represents a 9.1% increase, from 2013. An increase of bonds payable was offset by decreases in vendor payables, unearned revenue, (previously deferred revenue), loans payable, bond fees payable, interest payable and leases payable during the year.

- Operating revenues increased by $284,225, which represents a 12.5% increase from 2013. This increase is a result of increased enrollment plus the collection of a full year of Casino tax revenues.

- Expenses increased by $305,599 which represents an 11.6% increase from 2013. Operating expense increases are due to increases in salaries, fringe benefits, services, materials, supplies and bond fees. Expense reductions occurred in the purchase of furniture and equipment and depreciation.

- Non-operating revenues decreased by $21,107, which represents a 4.6% decrease from 2013. This decrease is due to reductions in federal grant programs.

## Using this Financial Report

This report consists of three parts, Management's Discussion and Analysis, the Financial Statements and the Notes to the Financial Statements. The Financial Statements include a Statement of Net Position, a Statement of Revenues, Expenses and Changes in Net Position and a Statement of Cash Flows.

**Statement of Net Position**

The Statement of Net Position looks at how well MDCE has performed financially through June 30, 2014. This statement includes all of the assets, deferred outflow of resources, liabilities and net position using the accrual basis of accounting, which is the accounting method used by most private-sector companies. This basis of accounting takes into account all revenues earned and expenses incurred during the year, regardless as to when the cash is received or expended.

The following schedule provides a summary Statement of Net Position for fiscal years ended June 30, 2014 and 2013 for MDCE.

| | 2014 | Restated 2013 | Change | % |
|---|---|---|---|---|
| **Assets** | | | | |
| Cash | $776,416 | $606,171 | $170,245 | 28.1% |
| Other Current Assets | 309,189 | 126,456 | 182,733 | 144.5% |
| Non-Current Assets | 285,449 | 513,185 | (227,736) | -44.4% |
| Capital Assets | 2,092,110 | 2,214,616 | (122,506) | -5.5% |
| Deferred Outflow of Resources | 330,424 | 0 | 330,424 | 100.0% |
| Total Assets and Deferred Outflow of Resources | 3,793,588 | 3,460,428 | 333,160 | 9.6% |
| **Liabilities** | | | | |
| Current Liabilities | 124,035 | 450,516 | (326,481) | -72.5% |
| Long-Term Liabilities | 3,148,439 | 2,548,830 | 599,609 | 23.5% |
| Total Liabilities | 3,272,474 | 2,999,346 | 273,128 | 9.1% |
| **Net Position** | | | | |
| Net Investment in Capital Assets | (322,859) | (295,293) | (27,566) | 9.3% |
| Net Restricted for Debt Purposes | 62,615 | 216,022 | (153,407) | -71.0% |
| Unrestricted | 781,358 | 540,353 | 241,005 | 44.6% |
| Total Net Position | $521,114 | $461,082 | $60,032 | 13.0% |

Net Position increased $60,032 in fiscal year 2014 due primarily to increased enrollment and increased collection of casino taxes. This was partially offset by reductions of federal grants, increases of operating expenses and bond issuance fees. Cash increased $170,245; bond escrow accounts increased $167,298; due from other governments decreased $2,739; accounts receivable increased $18,175; bond reserve accounts decreased $227,737; deferred outflow of resources increased $330,424 and net capital assets decreased $122,506 from 2013. Accounts payable decreased $13,500; interest payable decreased $40,849; loans payable decreased $257,475; unearned revenue (previously deferred revenues) decreased $975; equipment leases payable decreased $44,538 and bonds payable increased $630,465 from 2013.

### Statement of Revenues, Expenses and Changes in Net Position

The Statement of Revenues, Expenses and Changes in Net Position reports operating and non-operating activities for the fiscal year ended June 30, 2014.

The following schedule provides a summary of the Statement of Revenues, Expenses and Changes in Net Position for MDCE for fiscal years ended June 30, 2014 and 2013.

| | 2014 | Restated 2013 | Change | % |
|---|---|---|---|---|
| **Revenues** | | | | |
| Foundation and Poverty Based Assistance Revenues | $2,458,167 | $2,215,908 | $242,259 | 10.9% |
| Other Operating Revenues | 96,709 | 54,743 | 41,966 | 76.7% |
| Total Operating Revenues | 2,554,876 | 2,270,651 | 284,225 | 12.5% |
| Federal and State Grants | 440,129 | 461,236 | (21,107) | -4.6% |
| Total Non-Operating Revenues | 440,129 | 461,236 | (21,107) | -4.6% |
| Total Revenues | 2,995,005 | 2,731,887 | 263,118 | 9.6% |
| **Expenses** | | | | |
| Salaries | 1,125,256 | 1,055,110 | 70,146 | 6.6% |
| Fringe Benefits | 345,191 | 317,441 | 27,750 | 8.7% |
| Purchased Services | 803,320 | 783,668 | 19,652 | 2.5% |
| Materials and Supplies | 109,246 | 93,488 | 15,758 | 16.9% |
| Capital Outlay | 18,016 | 23,614 | (5,598) | -23.7% |
| Depreciation | 113,842 | 115,264 | (1,422) | -1.2% |
| Other Expenses | 420,102 | 240,789 | 179,313 | 74.5% |
| Total Expenses | 2,934,973 | 2,629,374 | 305,599 | 11.6% |
| Changes in Net Position | 60,032 | 102,513 | (42,481) | -41.4% |
| Net Position: Beginning of the Year | 461,082 | 358,569 | 102,513 | 28.6% |
| Net Position: End of Year | $521,114 | $461,082 | $60,032 | 13.0% |

Net Position increased in both fiscal years ended June 30, 2014 and 2013. This is due to increased enrollment, changes in federal grant programs, and improved operating efficiencies. Fees to refinance the 2008 bond issue totaled $158,879 in 2014. Although certain expenditures such as salaries will increase or decrease as the number of classes increase and decrease other costs remain fixed such as facilities costs resulting in more efficient operations. Additionally, grants have been received for capital improvements to our building and to purchase various educational programs and equipment.

Overall, revenues increased by $263,118 from 2013 to 2014. The most significant changes in revenues are an increase of $232,612 in State Foundation and Poverty Based Assistance funds, $9,646 in Casino Tax revenues and decreased Federal Funds totaling $21,433. Other revenues increased mostly due to miscellaneous other items.

Total expenses increased $305,599 from 2013 to 2014. Salaries and Fringe Benefits increased $97,896 due to staff increases and regular annual increases. Purchased services increased $19,652 due to administrative services and occupancy costs. Materials and Supplies increased $15,758 due to increased purchases of software and text books. Capital Outlay decreased $5,598 due to reduced purchases of furniture and equipment for classrooms. Depreciation decreased $1,422. Other Expenses increased $179,313 due to increased bond fee expenses.

**Capital Assets**

As of June 30, 2014, MDCE had $2,092,110 invested in land, building, building improvements, technology, software, furniture and equipment, net of depreciation. This is a $122,506 decrease from June 30, 2013. The following schedule provides a summary of Capital Assets as of June 30, 2014 and 2013 for MDCE.

| | 2014 | 2013 | Change | % |
|---|---|---|---|---|
| **Capital Assets (net of depreciation)** | | | | |
| Land | $80,000 | $80,000 | $0 | 0.0% |
| Building | 603,000 | 621,000 | (18,000) | -2.9% |
| Building Improvements | 1,300,806 | 1,339,056 | (38,250) | -2.9% |
| Technology and Software | 69,072 | 127,476 | (58,404) | -45.8% |
| Furniture and Equipment | 39,232 | 47,084 | (7,852) | -16.7% |
| Net Capital Assets | $2,092,110 | $2,214,616 | ($122,506) | -5.5% |

For more information on capital assets see the Notes to the Financial Statements.

## Bond Debt Service

On April 10, 2014 MDCE shared in the closing of a multi-school, multi-property bond financing arrangement with the Cleveland Cuyahoga County Port Authority (CCCPA). A portion of the proceeds, along with escrow and reserve deposits from a 2008 bond issue, were deposited into an escrow account with US Bank, National Association for the purpose of advance refunding the prior bonds when they come due. The CCCPA bond refinance allowed MDCE to acquire title to the land and building in which it operates, to improve ongoing financial reporting requirements and to complete renovation projects at MDCE. MDCE provided a mortgage on the land, building and improvements from US Bank, National Association. Financing was achieved through the issuance of a series of bonds maturing annually beginning on January 1, 2015 and continuing until January 1, 2044. Interest, which is paid semi-annually on January 1 and July 1, varies from a rate of 5.00% per annum to 7.75%.The outstanding principal balance, net of unamortized original bond discount, as of June 30, 2014 is $3,136,725. For more information on debt service see the Notes to the Financial Statements.

## Equipment Financing

During fiscal year 2012 MDCE entered into a lease agreement with Winthrop Resources Corporation for $179,855 worth of technology equipment. The lease value has been recorded as capital equipment to recognize the asset, and as capital equipment lease payable to recognize the lease debt. The lease term is for a total of 48 months, carries an interest rate of 7.38% per annum and will expire in January 2016 at which time the equipment will have minimal value. The outstanding principal value as of June 30, 2014 on the lease payable is $77,574.

## Current Financial Issues

Constellation Schools: Madison Community Elementary opened in the fall of 2004. The school has grown from 35 students, three teaching staff members and expenses of $387,165 to a total of 314 students, 29 teaching staff members and expenses of $2,934,973. MDCE exercised its' purchase option and arranged for the sale of the building and land which it leased to The Industrial Development Authority of the County of Pima. Title to the property was transferred to MDCE during 2014 as part of the bond refinancing with the CCCPA.

As the nation continues to recover from a major economic downturn, the Board of Directors, school management and school staff have worked diligently to ensure that the school maintains the high level of educational services and financial integrity that we have always provided. Our goal is to provide a strong educational product for our students and families and to maintain the reputation we have developed during our previous years.

## Contacting the School's Financial Management

This financial report is designed to provide our constituents with a general overview of the finances for MDCE and to show accountability for the monies it receives. If you have any questions about this report or need additional information please contact Thomas F. Babb, M.A., CPA by mail at Constellation Schools LLC, 5730 Broadview Road, Parma, Ohio 44134; by e-mail at babb.thomas@constellationschools.com; by calling 216.712.7600; or by faxing 216.712.7601.

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**Constellation Schools: Madison Community Elementary**
**Cuyahoga County, Ohio**
**Statement of Net Position**
**As of June 30, 2014**

| | |
|---|---|
| ***Assets:*** | |
| ***Current Assets:*** | |
| Cash | $776,416 |
| Escrow Accounts | 275,411 |
| Accounts Receivable | 21,332 |
| Due from Other Governments | 12,446 |
| *Total Current Assets* | 1,085,605 |
| ***Non-Current Assets:*** | |
| Security Deposit | 29,339 |
| Bond Reserve Accounts | 256,110 |
| Non-Depreciable Capital Assets | 80,000 |
| Capital Assets (Net of Accumulated Depreciation) | 2,012,110 |
| *Total Non-Current Assets* | 2,377,559 |
| *Total Assets* | 3,463,164 |
| ***Deferred Outflow of Resources:*** | |
| Unamortized Deferred Charges on Bond Refinancing | 330,424 |
| *Total Deferred Outflow of Resources* | 330,424 |
| *Total Assets and Deferred Outflow of Resources* | 3,793,588 |
| ***Liabilities:*** | |
| ***Current Liabilities:*** | |
| Accounts Payable | 9,125 |
| Interest Payable | 46,855 |
| Unearned Revenue | 2,195 |
| Capital Lease Equipment Payable | 47,938 |
| Capital Lease Bond Notes Payable | 17,922 |
| *Total Current Liabilities* | 124,035 |
| ***Long Term Liabilities:*** | |
| Capital Lease Equipment Payable | 29,636 |
| Capital Lease Bond Notes Payable | 3,118,803 |
| *Total Long Term Liabilities* | 3,148,439 |
| *Total Liabilities* | 3,272,474 |
| ***Net Position:*** | |
| Net Investment in Capital Assets | (322,859) |
| Net Restricted for Debt Purposes | 62,615 |
| Unrestricted | 781,358 |
| *Total Net Position* | $521,114 |

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

**Constellation Schools: Madison Community Elementary**
**Cuyahoga County, Ohio**
**Statement of Revenues, Expenses and**
**Changes in Net Position**
**For the Fiscal Year Ended June 30, 2014**

| | |
|---|---|
| ***Operating Revenues:*** | |
| Foundation and Poverty Based Assistance Revenues | $2,458,167 |
| Other Operating Revenues | 96,709 |
| *Total Operating Revenues* | 2,554,876 |
| | |
| ***Operating Expenses:*** | |
| Salaries | 1,125,256 |
| Fringe Benefits | 345,191 |
| Purchased Services | 803,320 |
| Materials and Supplies | 109,246 |
| Capital Outlay | 18,016 |
| Depreciation | 113,842 |
| Other Operating Expenses | 66,262 |
| *Total Operating Expenses* | 2,581,133 |
| | |
| Operating Loss | (26,257) |
| | |
| ***Non-Operating Revenues & Expenses:*** | |
| Interest Expense | (194,961) |
| Bond Issuance Fees | (158,879) |
| Federal and State Grants | 440,129 |
| *Total Non-Operating Revenues & Expenses* | 86,289 |
| | |
| Change in Net Position | 60,032 |
| | |
| Net Position at Beginning of the Year - Restated (See Note II.3) | 461,082 |
| | |
| Net Position at End of Year | $521,114 |

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

**Constellation Schools: Madison Community Elementary**
**Cuyahoga County, Ohio**
**Statement of Cash Flows**
**For the Fiscal Year Ended June 30, 2014**

| | |
|---|---|
| **Increase (Decrease) in Cash:** | |
| | |
| **Cash Flows from Operating Activities:** | |
| Cash Received from State of Ohio | $2,458,167 |
| Cash Payments to Suppliers for Goods and Services | (1,363,865) |
| Cash Payments to Employees for Services | (1,125,256) |
| Other Operating Revenues | 95,734 |
| Net Cash Provided by Operating Activities | 64,780 |
| | |
| **Cash Flows from Noncapital Financing Activities:** | |
| Federal and State Grants Received | 444,356 |
| Net Cash Provided by Noncapital Financing Activities | 444,356 |
| | |
| **Cash Flows from Capital and Related Financing Activities:** | |
| Payments for Capital Acquisitions | (2,669) |
| Bond Issuance Fees | (158,879) |
| Bond Issue Proceeds | 3,153,341 |
| Bond Issue Discount | (16,789) |
| Increase in Escrow Funds | (167,298) |
| Decrease in Bond Reserve Accounts | 227,737 |
| Payment to Escrow Agent | (2,805,120) |
| Bond Principal Payment | (35,005) |
| Bond Interest Payments | (216,826) |
| Loan Principal Payments | (257,475) |
| Loan Interest Payments | (7,846) |
| Equipment Lease Principal Payments | (44,538) |
| Equipment Lease Interest Payments | (7,524) |
| Net Cash Used for Capital and Related Financing Activities | (338,891) |
| | |
| Net Increase in Cash | 170,245 |
| Cash at Beginning of Year | 606,171 |
| | |
| Cash at End of Year | $776,416 |

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

**Constellation Schools: Madison Community Elementary**
**Cuyahoga County, Ohio**
**Statement of Cash Flows**
**For the Fiscal Year Ended June 30, 2014**
**(Continued)**

| | |
|---|---|
| **Reconciliation of Operating Loss to Net Cash Provided by Operating Activities:** | |
| Operating Loss | ($26,257) |
| **Adjustments to Reconcile Operating Loss to Net Cash Provided by Operating Activities:** | |
| Depreciation and Amortization | 113,842 |
| Capital Asset Returned for Refund | 11,332 |
| Changes in Assets and Liabilities: | |
| (Increase) in Accounts Receivable | (18,175) |
| Decrease in Due from Other Governments | (1,488) |
| (Decrease) in Accounts Payable | (13,499) |
| (Decrease) in Unearned Revenue | (975) |
| Total Adjustments | 91,037 |
| Net Cash Provided by Operating Activities | $64,780 |

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

## I. Description of the School and Reporting Entity

Constellation Schools: Madison Community Elementary (MDCE) is a nonprofit corporation established December 5, 2003 pursuant to Ohio Revised Code Chapters 3314 and 1702 to maintain and provide a school exclusively for any educational, literary, scientific and related teaching service that qualifies as an exempt organization under §501(c)(3) of the Internal Revenue Code. On March 28, 2006, MDCE received a determination letter confirming tax-exempt status with the Internal Revenue Service under section 501(c)(3) of the Internal Revenue Code. Management is not aware of any course of action or series of events that have occurred that might adversely affect the tax-exempt status of MDCE. MDCE, which is part of Ohio's education program, is independent of any school district. MDCE may sue and be sued, acquire facilities as needed, and contract for any services necessary for the operation of MDCE.

MDCE was approved for operation as Madison Community School on January 20, 2004 under a contract between the Governing Authority of MDCE and Lucas County Educational Service Center (LCESC) as their sponsor. The contract with LCESC, now known as ESC of Lake Erie West (ESCLEW) has been renewed with a current expiration date of June 30, 2017. Under the terms of the contract ESCLEW will provide sponsorship services for a fee. For further discussion of the sponsor services see Note XV.

MDCE entered into an agreement with Constellation Schools (CS) to provide legal, financial, business and educational management services for the fiscal year. See Note XV for further discussion of this management agreement.

MDCE operates under a five member Board of Directors. The Board is responsible for carrying out the provisions of the contract, which include, but are not limited to, state mandated provisions regarding student population, curriculum, academic goals, performance standards, admission standards, and qualification of teachers. The Board of Directors controls MDCE' instructional facility staffed by twenty-nine certificated full time teaching personnel and eight support staff who provide services to 314 students. During 2014, the board members for MDCE also serve as the board for Constellation Schools: Westpark Community Elementary, Constellation Schools: Mansfield Community Elementary, Constellation Schools: Puritas Community Elementary and Constellation Schools: Stockyard Community Elementary.

## II. Summary of Significant Accounting Policies

The financial statements of MDCE 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 more significant of MDCE's accounting policies are described below.

## 1. 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. Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment is determined by its measurement focus. Enterprise accounting uses a flow of economic resources measurement focus. With this measurement focus, all assets, deferred outflow of resources and all liabilities are included on the Statement of Net Position. Operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total position.

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. MDCE prepares financial statements using the accrual basis of accounting. Revenues resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded when the exchange takes place. Revenues resulting from non-exchange transactions, in which MDCE receives value without directly giving equal value in return, such as grants and entitlements, are recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include timing requirements, which specify the fiscal year when the resources are required to be used or the fiscal year when the use is first permitted; matching requirements, in which MDCE must provide local resources to be used for a specified purpose; and expenditure requirements, in which resources are provided to MDCE on a reimbursement basis. Expenses are recognized at the time they are incurred.

## 3. Change in Accounting Principles

For 2014, MDCE has implemented GASB Statement No. 65, "*Items Previously Reported as Assets and Liabilities".* GASB Statement No. 65 establishes accounting and financial reporting standards that reclassify, as *deferred outflows of resources* or *deferred inflows of resources*, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. GASB Statement No. 65 also provides other financial reporting guidance related to the impact of the financial statement elements *deferred* *outflows of resources* and *deferred inflows of resources,* such as changes in the determination of the major fund calculations and limiting the use of the term *deferred* in financial statement presentations. The implementation of GASB Statement No. 65 had the following effect on the financial statements of MDCE as follows:

| | |
|---|---|
| Net Position Previously Reported as of June 30, 2013 | $717,878 |
| Removal of Unamortized Bond Issuance Costs | (256,796) |
| Restated Net Position at July 1, 2013 | $461,082 |

**4. Cash**

All monies received by MDCE are deposited in demand deposit accounts.

**5. Budgetary Process**

Pursuant to Ohio Revised Code Chapter 5705.391 MDCE prepares and adopts an annual budget which includes estimated revenues and expenditures for the fiscal year and a five year forecast of revenues and expenditures. MDCE will from time to time adopt budget revisions as necessary.

**6. Due From Other Governments and Accounts Receivable**

Monies due MDCE for the year ended June 30, 2014 are recorded as Due From Other Governments and as Accounts Receivable. A current asset for the receivable amount is recorded at the time of the event causing the monies to be due.

**7. Capital Assets and Depreciation**

Capital assets are capitalized at cost and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market values as of the dates received. All items with a useful life of one year or greater and a value of $1,000 or more 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.

All capital assets are depreciated except for land. Depreciation of buildings, building improvements, computers, technology and furniture and equipment is computed using the straight line method over their estimated useful lives. Improvements to fixed assets are depreciated over the remaining useful lives of the related fixed assets or less. Estimated useful lives are as follows:

| Capital Asset Classification | Years |
|---|---|
| Building | 40 |
| Building Improvements | 10 to 40 |
| Technology & Software | 3 to 5 |
| Furniture and Equipment | 10 |

### 8. Intergovernmental Revenues

MDCE currently participates in the State Foundation Program, the State Poverty Based Assistance Program and Casino Tax Distribution. Revenues received from these programs are recognized as operating revenues in the accounting period in which all eligibility requirements have been met. MDCE also participates in Federal Entitlement Programs, the Federal Lunch Reimbursement Program, Race to the Top and various State Grant Programs. State and Federal Grants and Entitlements are recognized as non-operating revenues in the accounting period in which all eligibility requirements have been met. Amounts awarded under the above named programs for the 2014 school year totaled $2,898,296.

### 9. Private Grants and Contributions

MDCE receives grants and contributions from private sources to support the schools programs. Private grants and contributions are recognized as non-operating revenues in the accounting period in which they are received. MDCE did not receive any grants and contributions for the 2014 school.

### 10. Compensated Absences

Vacation is taken in a manner which corresponds with the school calendar; therefore, MDCE does not accrue vacation time as a liability.

Sick leave benefits are earned at the rate of one and one-quarter day per month and can be accrued up to a maximum of one hundred twenty days. MDCE will accept the transfer of sick days from another school district up to the maximum accrual amount. No financial accrual for sick time is made since unused sick time is not paid to employees upon employment termination.

### 11. Use of 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.

### 12. Unearned Revenue

Unearned revenue arises when assets are recognized before revenue recognition criteria have been satisfied. The unearned revenue for MDCE consists of materials fees received in the current year which pertains to the next school year.

### 13. Deferred Inflows of Resources and Deferred Outflows of Resources

A deferred inflow of resources is an acquisition of assets by the school that is applicable to a future reporting period. A deferred outflow of resources is a consumption of assets by the school that is applicable to a future reporting period. When utilizing the accrual basis of accounting, unamortized deferred charges on debt refinancing are reported as a deferred outflow of resources. A deferred charge on refunding results from the difference in the carrying value of the refunded debt and its' reacquisition price. This amount is deferred and amortized over the shorter period of the life of the refunded debt or of the refunding debt.

## III. Deposits

At fiscal year end June 30, 2014, the carrying amount of MDCE's deposits totaled $776,416 and its bank balance was $803,691. Based on the criteria described in GASB Statement No. 40, "Deposit and Investment Risk Disclosure," as of June 30, 2014, $508,085, of the bank balance was exposed to custodial risk as discussed below, while $295,606 was covered by the Federal Depository Insurance Corporation.

Escrow and reserve accounts held in trust on behalf of MDCE and the Cleveland Cuyahoga County Port Authority totaled $531,521 at fiscal year end June 30, 2014. The escrow accounts are invested in the US Treasury and are 100% backed by the full faith and credit of the United States government. Reserve accounts are invested in U.S. Bank Open Commercial Paper instruments.

Custodial credit risk is the risk that in the event of bank failure, MDCE will not be able to recover the deposits. All deposits are collateralized with eligible securities in amounts equal to at least 105% of the carrying value of the deposits. Such collateral, as permitted by the Ohio Revised Code, is held in single financial institution collateral pools at the Federal Reserve Banks or at member banks of the federal reserve system, in the name of the respective depository bank and pledged as a pool of collateral against all of the public deposits it holds or as specific collateral held at the Federal Reserve Bank in the name of MDCE.

## IV. Capital Assets

A summary of capital assets at June 30, 2014 follows:

| | Balance 6/30/13 | Additions | Deletions | Balance 6/30/14 |
|---|---|---|---|---|
| Capital Assets Not Being Depreciated: | | | | |
| Land | $80,000 | $0 | $0 | $80,000 |
| Capital Assets Being Depreciated: | | | | |
| Building | 720,000 | 0 | 0 | 720,000 |
| Building Improvements | 1,497,356 | 0 | 0 | 1,497,356 |
| Technology and Software | 262,409 | 0 | (11,332) | 251,077 |
| Furniture and Equipment | 102,990 | 2,669 | 0 | 105,659 |
| Total Capital Assets Being Depreciated | 2,582,755 | 2,669 | (11,332) | 2,574,092 |
| Less Accumulated Depreciated: | | | | |
| Building | (99,000) | (18,000) | 0 | (117,000) |
| Building Improvements | (158,300) | (38,250) | 0 | (196,550) |
| Technology and Software | (134,934) | (47,071) | 0 | (182,005) |
| Furniture and Equipment | (55,906) | (10,521) | 0 | (66,427) |
| Total Accumulated Depreciation | (448,140) | (113,842) | 0 | (561,982) |
| Capital Assets Being Depreciated, Net of Accumulated Depreciation | 2,134,615 | (111,173) | (11,332) | 2,012,110 |
| Total Capital Assets, Net of Accumulated Depreciation | $2,214,615 | ($111,173) | ($11,332) | $2,092,110 |

## V. Purchased Services

Purchased Services include the following:

| | |
|---|---|
| Instruction | $70,536 |
| Pupil Support Services | 128,299 |
| Staff Development & Support | 39,268 |
| Administrative | 373,323 |
| Occupancy Costs | 82,968 |
| Food Services | 107,648 |
| Student Activities | 1,278 |
| Total Purchased Services | $803,320 |

## VI. Capital Equipment Lease Payable

During fiscal year 2012, MDCE entered into a four year lease for technology equipment. This lease meets the criteria of a capital lease as defined by accounting standards, which defines a capital lease generally as one which transfers the benefits and risks of ownership of the lessee.

Assets of technology equipment totaling $179,855 have been capitalized. This amount represents the actual purchase price of the equipment and is the same as the net present value of the minimum lease payments at the time of acquisition. Principal payments during fiscal year 2014 totaled $44,538 and interest paid totaled $7,524. Future minimum lease payments for principal and interest under the capital lease are as follows:

| Year | Principal | Interest | Total |
|---|---|---|---|
| 2015 | $47,938 | $4,124 | $52,062 |
| 2016 | 29,636 | 735 | 30,371 |
| Total | $77,574 | $4,859 | $82,433 |

## VII. School Building Purchase

In order to finance a multi-million dollar expansion project during fiscal year 2008 the building and land located at West 98$^{th}$ and Madison in Cleveland was purchased by The Industrial Development Authority of the County of Pima (IDA) on January 23, 2008 as part of a bond financing deal. MDCE leased the property from IDA under a capitalized lease arrangement. On April 10, 2014 the bond issue was refinanced and title for the property was turned over to the ownership of MDCE (See Note VIII). The original purchase price and building improvements under the capitalized lease continue to be recognized as capital assets and are being depreciated over their remaining useful life.

## VIII. Capital Lease Bond Notes Payable

On April 10, 2014 MDCE closed a $30,790,000 multi-school, multi-property bond financing arrangement with the Cleveland Cuyahoga County Port Authority (CCCPA). Underwriters' discounts totaling $538,825 and original bond discounts of $163,934 were deducted from the bond proceeds at issuance. A portion of the proceeds, along with escrow and reserve deposits from a prior bond issue, were deposited into an escrow account with US Bank, National Association for the purpose of advance refunding the prior bonds when they come due (See Note IX). In addition, $4,953,849 of the CCCPA bonds is financing multi-million dollar building acquisition, renovation and expansion projects to meet increasing demand for enrollment for the participating schools.

The properties are managed through annual lease and sub-lease arrangements. MDCE and the CCCPA secured mortgages on the land, building and improvements from US Bank, National Association. Financing was achieved through the issuance of a series of bonds maturing annually beginning on January 1, 2015 and continuing until January 1, 2044. Interest, which is paid semi-annually on January 1 and July 1, is at the rate of 5.00% per annum for the bonds maturing between 2015 and 2017 (Series B); 5.75% for the bonds maturing between 2018 and 2024 (Series A); 6.50% for the bonds maturing between 2025 and 2034(Series A); and 7.75% for the bonds maturing between 2035 and 2044 (Series A). The outstanding principal balance, net of unamortized bond discount, as of June 30, 2014 is $3,136,725 and interest payable due July 1, 2014 is $46,378. Interest expense during 2014 totaled $179,865. Changes in the Capital Lease Bond Notes Payable during the year consist of the following:

| | Balance 6/30/13 | Additions | Reductions | Balance 6/30/14 | Due In One Year |
|---|---|---|---|---|---|
| 2008 Bonds | $2,506,260 | $0 | ($2,506,260) | $0 | $0 |
| 2014 Bonds: | | | | | |
| Series A | 0 | 3,070,385 | 0 | 3,070,385 | 0 |
| Series B | 0 | 82,956 | 0 | 82,956 | 17,922 |
| Bond Discount | 0 | (16,789) | 173 | (16,616) | 0 |
| TOTALS | $2,506,260 | $3,136,552 | ($2,506,087) | $3,136,725 | $17,922 |

These lease obligations meet the criteria of a capital lease as defined by Financial Accounting Standards Board Statement Number 13, "Accounting for Leases" and has been recorded in the financial statements. Land, Building, Other Purchase Costs, and Building Improvements in existence at the date of the bond issuance continue to be recognized as capital assets and are being depreciated over their remaining useful life.

MDCE's share of bond issuance costs totaling $158,879 were expensed at the time of the bond issuance. The reacquisition price exceeded the net carrying amount of the 2008 debt by $333,866. Loss on refinancing is reported as "Unamortized Deferred Charges on Bond Refinancing" and is being amortized through annual charges to interest for the remaining life of the 2008 bond issue. The original bond discount, which totaled $16,789 for MDCE, is being amortized through annual charges to interest for the remaining life of the 2008 bond issue. As of June 30, 2014 the unamortized balances for the cost to refinance and the bond discount are $330,424 and $16,616 respectively. The Bond Indenture requires MDCE to meet certain covenants. As of June 30, 2014 MDCE is in compliance with those covenants.

As part of the agreements for the leases, monies were deposited into several escrow accounts with US Bank, N.A. Payments for renovation and financing activities have been paid from these accounts through June 30, 2014. Lease payments were made by MDCE to cover bond interest and administrative fees and to make deposits into reserve accounts. Funds were deposited from initial bond proceeds into a Debt Service Reserve Account to meet future debt service needs. Lease payments made during 2014 to fund interest, reserves and bond expenses totaled $149,261. The balances of escrow and reserve accounts as of June 30, 2014 are as follows:

| | |
|---|---|
| Project Fund | $217,777 |
| Bond Debt Service Account | 52,831 |
| Expense Fund | 4,803 |
| Total Bond Escrow Accounts | $275,411 |
| | |
| Debt Service Reserve | $252,000 |
| Operating Reserve | 4,110 |
| Total Bond Reserve Accounts | $256,110 |

The assets refinanced and through the capital lease as of June 30, 2014 are as follows:

| | |
|---|---|
| Land | $80,000 |
| Building | 720,000 |
| Building Improvements | 1,497,356 |
| Sub-Total | 2,297,356 |
| Accumulated Depreciation | (313,550) |
| Net Book Value | $1,983,806 |

Future minimum lease payments for principal and interest on the face value of the Series 2014 bonds (does not include amortization of the loss to refinance the Series 2008 bonds or the bond discount on the Series 2014 bonds) under the capital lease are as follows:

| Year | Principal | Interest | Total |
|---|---|---|---|
| 2015 | $17,922 | $148,969 | $166,891 |
| 2016 | 31,748 | 204,578 | 236,326 |
| 2017 | 33,286 | 202,991 | 236,277 |
| 2018 | 34,821 | 201,326 | 236,147 |
| 2019 | 36,869 | 199,324 | 236,193 |
| 2020 - 2024 | 288,809 | 954,722 | 1,243,531 |
| 2025 - 2029 | 390,199 | 855,591 | 1,245,790 |
| 2030 - 2034 | 537,676 | 710,769 | 1,248,445 |
| 2035 - 2039 | 744,041 | 507,689 | 1,251,730 |
| 2040 - 2044 | 1,037,970 | 219,487 | 1,257,457 |
| Total | $3,153,341 | $4,205,446 | $7,358,787 |

## IX. Refunded Capital Lease Bond Notes Payable

On April 10, 2014 MDCE closed a $30,790,000 multi-school, multi-property bond financing arrangement with the Cleveland Cuyahoga County Port Authority (CCCPA). A portion of the proceeds, $22,004,213, along with escrow and reserve deposits from a prior bond issue, $5,245,493, were used to advance refund the entire Constellation Schools Series 2008 Bonds issued by The Industrial Development Authority of the County of Pima (See Note VIII). The refunding portion of the issue, along with the escrow and reserve accounts from the 2008 issue, were deposited into an escrow account with US Bank, National Association for the purpose of advance refunding the bonds when they come due.

## X. Loans Payable

On June 30, 2011 MDCE executed two unsecured promissory notes with Constellation Schools: Westpark Community Elementary and Constellation Schools: Puritas Community Elementary in the amount of $200,000 to each school for a total of $400,000. Each note carries interest at 4% per annum. Interest only was charged through September 30, 2011 at which time interest and principal payments began. Payments are based on a five year amortization schedule with a balloon payment for the principal balance due at June 30, 2014. The notes were paid in full as part of the bond refinancing that occurred on April 10, 2014 (See Note VIII).

## XI. Risk Management

### 1. Property and Liability Insurance

MDCE 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 2014, MDCE contracted with Traveler's Property Casualty Company of America for property insurance, The Hanover Insurance Company for liability insurance and errors and omissions insurance and Allamerica Financial Benefit Insurance Company for Automobile insurance.

General property and liability is covered at $10,000,000 single occurrence limit and $11,000,000 aggregated. Hired and Non-Owned Vehicles are covered at $1,000,000 combined single limit of liability. Other coverage includes Employee Crime, School Leaders Errors & Omissions, Sexual Abuse and Misconduct, Electronic Data Processing and Business Interruption. Settled claims have not exceeded this coverage in any of the past three years, nor has there been any significant reduction in insurance coverage from the prior year.

### 2. Workers' Compensation

MDCE makes premium payments to the Ohio Worker's Compensation System for employee injury coverage. There have been six claims filed by MDCE employees with the Ohio Worker's Compensation System between January 1, 2010 and June 30, 2014. The total payments made for this claim have been $34,870. In the opinion of management, these claims will not have a material adverse effect on the overall financial position of MDCE as June 30, 2014.

### 3. Employee Medical, Dental, Vision and Life Benefits

MDCE provides medical, dental, vision and life insurance benefits to all full time employees. Employees participate in premium payments through pretax payroll deductions. Total insurance benefits paid by MDCE for the fiscal year is $154,818.

## XII. Defined Benefit Pension Plans

### 1. State Teachers Retirement System

MDCE 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 comprehensive annual financial report that may be obtained by writing to STRS

Ohio, 275 E. Broad St., Columbus, Ohio 43215-3371, by calling toll-free 1-888-227-7877, or by visiting the STRS website at www.strsoh.org.

New members have a choice of three retirement plan options. In addition to the Defined Benefit (DB) Plan, new members are offered a Defined Contribution (DC) Plan and a Combined Plan. The DC Plan allows members to allocate all their member contributions and employer contributions equal to 10.5% of earned compensation among various investment choices. The Combined Plan offers features of the DC Plan and the DB Plan. In the Combined Plan, member contributions are allocated to investment choices by the member, and employer contributions are used to fund a defined benefit payment at a reduced level from the regular DB Plan. Contributions into the DC Plan and the Combined Plan are credited to member accounts as employers submit their payroll information to STRS Ohio, generally on a biweekly basis. DC and Combined Plan members will transfer to the DB plan during their fifth year of membership unless they permanently select the DC or Combined Plan.

The DB Plan benefits are established under Chapter 3307 of the Ohio Revised Code. Any member may retire who has (i) five years of service credit and attained age 60; (ii) 25 years of service credit and attained age 55; or (iii) 30 years of service credit regardless of age. The annual retirement allowance, payable for life, is the greater of the "formula benefit" or the "money-purchase benefit" calculation. Under the "formula benefit," the retirement allowance is based on years of credited service and final average salary, which is the average of the members' three highest salary years. The annual allowance is calculated by using a base percentage of 2.2% multiplied by the total number of years of service credit (including Ohio-valued purchased credit) times the final average salary. The 31$^{st}$ year of earned Ohio service credit is calculated at 2.5%. An additional one-tenth of a percent is added to the calculation for every year of earned Ohio service over 31 years until 100% of the final average salary is reached. For members with 35 or more years of Ohio contributing service, the first 30 years will be calculated at 2.5% instead of 2.2%. Under the "money-purchase benefit" calculation, a member's lifetime contributions plus interest at specified rates are matched by an equal amount from other STRS Ohio funds. The total is then divided by an actuarially determined annuity factor to determine the maximum annual retirement allowance. Benefits are increased annually by 3% of the original base amount for DB Plan participants.

DC Plan benefits are established under Sections 3307.80 to 3307.89 of the Ohio Revised Code. For members who select the DC Plan, all member contributions and employer contributions at a rate of 10.5% are placed in an investment account. The member determines how to allocate the member and employer money among various investment choices. A member is eligible to receive a retirement benefit at age 50 and termination of employment. The member may elect to receive a lifetime monthly annuity or a lump sum withdrawal. Employer contributions into members' accounts are vested after the first anniversary of the first day of paid service. Members in the DC Plan who become disabled are entitled only to their account balance. If a member dies before retirement benefits begin, the members' designated beneficiary is entitled to receive the member's account balance.

Member contributions in the Combined Plan are allocated by the member, and employer contributions are used to fund a defined benefit payment. A members' defined benefit is determined by multiplying 1% of the members' final average salary by the members' years of service credit. The defined portion of the Combined Plan is payable to a member on or after age 60. The defined contribution portion of the account may be taken as a lump sum or converted to a lifetime monthly annuity at age 50.

A retiree of STRS Ohio or another Ohio public retirement system is eligible for reemployment following the elapse of two months from the date of retirement. Contributions are made by the reemployed member and employer during reemployment. Upon termination of reemployment or age 65, whichever comes later, the retiree is eligible for an annuity benefit or equivalent lump-sum payment in addition to the original retirement allowance. A reemployed retiree may alternatively receive a refund of only member contributions with interest before age 65, once employment is terminated.

The DB and Combined Plan offer access to health coverage to eligible retirees who participated in the plans and their eligible dependents. Coverage under the current program includes hospitalization, physicians' fees, prescription drugs and partial reimbursement of monthly Medicare Part B premiums. By Ohio law, health care benefits are not guaranteed.

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 members who die before retirement may qualify for survivor benefits. A death benefit of $1,000 is payable to the beneficiary of each deceased retired member who participated in the DB Plan. Death benefit coverage up to $2,000 can be purchased by participants in the DB, DC or Combined Plans. Various other benefits are available to members' beneficiaries.

Chapter 3307 of the Ohio Revised Code provides statutory authority for member and employer contributions. Contribution rates are established by the State Teachers Retirement Board, upon recommendation of its consulting actuary, not to exceed statutory maximum rates of 14% for members and 14% for employers. Contribution requirements and the contributions actually made for the fiscal year ended June 30, 2014, were 11% of covered payroll for members and 14% for employers. The amount required to fund pension obligations during the year is 13%.

MDCE's required contributions for pension obligations for the fiscal years ended June 30, 2014, 2013 and 2012 were $126,755, $127,294 and $146,017 respectively; 100% has been contributed for fiscal years 2014, 2013 and 2012. Member and employer contributions actually made for DB, DC and Combined Plan participants will be provided upon written request.

**2. School Employees Retirement System**

MDCE contributes to the School Employees Retirement System of Ohio (SERS), a cost-sharing, multiple-employer defined benefit pension plan. SERS provides retirement, disability and survivor benefits; annual cost-of-living adjustments; and death benefits to plan members and beneficiaries. Authority to establish and amend benefits is provided by state statute per Chapter 3309 of the Ohio Revised Code. SERS issues a publicly available, stand-alone financial report that includes financial statements and required supplementary information. The report can be obtained on SERS' website at www.ohsers.org under Employers/Audit Resources.

Plan members are required to contribute 10% of their annual covered salary and MDCE is required to contribute 14% of annual covered payroll. The contribution requirements of plan members and employers are established and may be amended, up to statutory maximum amounts, by the SERS' Retirement Board. The Retirement Board acting with the advice of the actuary, allocates the employer contribution rate among four of the funds (Pension Trust Fund, Death Benefit Fund, Medicare B Fund and Health Care Fund) of the System. For fiscal year ending June 30, 2014, the allocation to pension and death benefits is 13.10%. The remaining 0.90% of the 14% employer contribution rate is allocated to the Health Care and Medicare B Funds. MDCE's contributions to SERS for the fiscal years ended June 30, 2014, 2013 and 2012 were $21,030, $10,630 and $12,108, respectively; 100% has been contributed for fiscal years 2014, 2013 and 2012.

## XIII. Post-Employment Benefits Other than Pension Benefits

**1. State Teachers Retirement System**

Ohio law authorizes STRS Ohio to offer a cost-sharing, multiple employer health care plans. STRS Ohio provides access to health care coverage to eligible retirees who participated in the Defined Benefit or Combined Plans. Coverage under the current program includes hospitalization, physicians' fees, prescription drugs and reimbursement of monthly Medicare Part B premiums.

Pursuant to Section 3307 of the Ohio Revised Code, the Retirement Board has discretionary authority over how much, if any, of the associated health care costs will be absorbed by STRS Ohio. All benefit recipients, for the most recent year, pay a portion of the health care costs in the form of a monthly premium.

Under Ohio law funding for post-employment health care may be deducted from employer contributions. Of the 14% employer contribution rate, 1% of covered payroll was allocated to post-employment health care. The 14% employer contribution rate is the maximum rate established under Ohio law. For the fiscal years ended June 30, 2014, 2013 and 2012 MDCE's contributions to post-employment health care were $9,750, $9,792 and $11,232, respectively; 100% has been contributed for fiscal years 2014, 2013 and 2012.

**2. School Employees Retirement System**

In addition to a cost-sharing multiple-employer defined benefit pension plan the School Employees Retirement System of Ohio administers two post-employment benefit plans. The Medicare B Plan reimburses Medicare Part B premiums paid by eligible retirees and beneficiaries as set forth in Ohio Revised Code 3309.69. Qualified benefit recipients who pay Medicare Part B premiums may apply for and receive a monthly reimbursement from SERS. The reimbursement amount is limited by statute to the lesser of the January 1, 1999 Medicare Part B premium or the current premium. The Medicare Part B premium for calendar year 2014 was $104.90 for most participants, but could be as high as $335.70 per month depending on their income. SERS' reimbursement to retirees was $45.50.

The Retirement Board, acting with the advice of the actuary, allocates a portion of the current employer contribution rate to the Medicare Part B Fund. For fiscal year 2014 the actuarially required allocation is .76%.For the fiscal years ended June 30, 2014, 2013 and 2012 MDCE contributions to Medicare Part B were $1,142, $562 and $657, respectively; 100% has been contributed for fiscal years 2014, 2013 and 2012.

Ohio Revised Code 3309.375 and 3309.69 permit SERS to offer health care benefits to eligible retirees and beneficiaries. SERS' Retirement Board reserves the right to change or discontinue any health plan or program. SERS offers several types of health plans from various vendors, including HMOs, PPOs, Medicare Advantage and traditional indemnity plans. A prescription drug program is also available to those who elect health coverage. SERS employs two third-party administrators and a pharmacy benefit manager to manage the self-insurance and prescription drug plans, respectively. The Ohio Revised Code provides a statutory authority to fund SERS' postemployment benefits through employee contributions. Active members do not make contributions to the postemployment plans.

The Health Care Fund was established under, and is administered in accordance with Internal Revenue Code 105(e). Each year after the allocation for statutorily required benefits, the Retirement Board allocates the remainder of the employer 14% contribution to the Health Care Fund. For the year ended June 30, 2014 the health care allocation is 0.14%. An additional health care surcharge on employers is collected for employees earning less than an actuarially determined minimum compensation amount, pro-rated according to service credit earned. Statutes provide that no employer shall pay a health care surcharge greater than 2% of that employer's SERS covered payroll; nor may SERS collect in aggregate more than 1.5% of the total statewide SERS-covered payroll for the health care surcharge. For fiscal year 2014, the minimum compensation level was established at $20,525. The surcharge, added to the unallocated portion of the 14% employer contribution rate is the total amount assigned to the Health Care Fund. For the fiscal years ended June 30, 2014, 2013 and 2012 MDCE contributions to the Health Care Plan, including the surcharge were $2,873, $1,452 and $2,544, respectively; 7.32% has been contributed for fiscal year 2014 and 100% for fiscal years 2013 and 2012. $2,663 representing the unpaid surcharge due for fiscal year 2014 is recorded as a liability within the respective funds.

## XIV. Contingencies

### 1. Grants

MDCE received financial assistance from Federal and State agencies in the form of grants. The disbursement of funds received under these programs 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 MDCE. However, in the opinion of management, any such disallowed claims will not have a material adverse effect on the overall financial position of MDCE at June 30, 2014.

### 2. Enrollment FTE

The Ohio Department of Education conducts reviews of enrollment and full-time equivalency (FTE) 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 conclusions of this review could result in state funding being adjusted. Adjustments to the state funding received during fiscal year 2014 are immaterial and are not reflected in the 2014 financial statements but will be included in the financial activity for fiscal year 2015.

## XV. Sponsorship and Management Agreements

MDCE entered into an agreement with the ESC of Lake Erie West, (ESCLEW) formerly Lucas County Educational Service Center, to provide sponsorship and oversight services as required by law. The agreement was renewed at the end of the fiscal year and continues until June 30, 2017. Sponsorship fees are calculated as 2.0% of the Fiscal Year 2014 Foundation payments received by MDCE, from the State of Ohio. The total amount due from MDCE for fiscal year 2014 was $48,266, all of which was paid prior to June 30, 2014.

MDCE entered into an agreement with Constellation Schools to provide legal, financial, and business management services for fiscal year 2014. The agreement was for a period of one year, effective July 1, 2010. Management fees are calculated as 6.25% of the Fiscal Year 2014 Foundation payment received by MDCE from the State of Ohio plus a fixed fee of $144,375. The total fee cannot exceed twice the fixed fee. The total amount due from MDCE for the fiscal year ending June 30, 2014 was $288,750 all of which was paid prior to June 30, 2014.

## XVI. Net Restricted for Debt Purposes

Net restricted for debt purposes represents the combination of Escrow Accounts and Bond Reserve Accounts, net of the outstanding portion of Bonds Payable used to finance these assets. The Project Fund, which is included in Escrow Accounts, is being held for construction purposes and was partially liquidated during the fiscal year. The Bond Debt Service Account and the Expense Fund, which are included in Escrow Accounts, along with the Debt Service Reserve and Operating Reserve Accounts, which are being held for bond financing reserve requirements, will continue to be funded until January 1, 2044.

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Rea & associates a brighter way

November 25, 2014

To the Board of Trustees
Constellation Schools: Madison Community Elementary
2015 West 95th Street
Cleveland, OH 44102

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

We have audited, in accordance with the 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, the financial statements of the Constellation Schools: Madison Community Elementary, Cuyahoga County, Ohio (the School), as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the School's basic financial statements, and have issued our report thereon dated November 25, 2014, wherein we noted the School implemented Governmental Accounting Standards Board (GASB) Statement No. 65 *"Items Previously Reported as Assets and Liabilities"* and restated their June 30, 2013 net position.

**Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the School's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the School's internal control. Accordingly, we do not express an opinion on the effectiveness of the School's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

**Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the School's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards.*

**Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the School's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Governmental Auditing Standards* in considering the School's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Rea & Associates, Inc.

Medina, Ohio

# Dave Yost • Auditor of State

**MADISON COMMUNITY ELEMENTARY**

**CUYAHOGA 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**
**DECEMBER 30, 2014**

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