DAYTON ACADEMY SCHOOL
MONTGOMERY COUNTY

REGULAR AUDIT

FOR THE YEAR ENDED JUNE 30, 2001

JIM PETRO
AUDITOR OF STATE
STATE OF OHIO

DAYTON ACADEMY SCHOOL
MONTGOMERY COUNTY

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REPORT OF INDEPENDENT ACCOUNTANTS

Dayton Academy School
Montgomery County
4401 Dayton-Liberty Rd.
Dayton, Ohio 45418

To the Board of Governance:

We have audited the accompanying balance sheet of the Dayton Academy School, Montgomery County, (the School), as of June 30, 2001, and the related Statement of Revenues, Expenses, and Changes in Retained Earnings/Accumulated Deficit and the Statement of Cash Flows for the year then ended. These financial statement are the responsibility of the School's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Dayton Academy School, Montgomery County, as of June 30, 2001, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 29, 2002, on our consideration of the School's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Jim Petro
Auditor of State

February 29, 2002

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DAYTON ACADEMY SCHOOL
MONTGOMERY COUNTY

BALANCE SHEET
AS OF JUNE 30, 2001

ASSETS

Current Assets	
Cash in Pooled Cash, Cash Equivalents	$ 777,012
Receivables:	
Intergovernmental	309,459
Other	13,601
Total Current Assets	1,100,072
Non-Current Assets	
Other Assets	6,594
Total Assets	1,106,666

LIABILITIES AND EQUITY

Current Liabilities	
Accounts Payable	33,519
Intergovernmental Payable	247,971
Accrued Edison Fees	396,254
Total Current Liabilities	677,744
Non-Current Liabilities	
Notes Payable	460,768
Total Liabilities	1,138,512
Equity	
Accumulated Deficit	(31,846)
Total Liabilities and Equity	$ 1,106,666

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

DAYTON ACADEMY SCHOOL
MONTGOMERY COUNTY

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN RETAINED EARNINGS/ACCUMULATED DEFICIT FOR THE YEAR ENDED JUNE 30, 2001

Operating Revenues	
State Foundation Payments	$ 3,702,676
Disadvantaged Pupil Impact Aid	609,022
Total Operating Revenues	4,311,698
Operating Expenses	
Fringe Benefits	105,564
Purchased Services	3,974,478
Depreciation and Amortization	3,816
Rent	455,977
Other Operating Expenses	229,145
Total Operating Expenses	4,768,980
Operating Loss	(457,282)
Non-Operating Revenues / (Expenses)	
Private Grants	2,396
Federal and State Grants	353,233
Loss on Sale of Equipment	(10,543)
Interest	48,028
Total Non-Operating Revenues / (Expenses)	393,114
Net Loss	(64,168)
Retained Earnings at Beginning of Year	32,322
Accumulated Deficit at End of Year	$ (31,846)

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

DAYTON ACADEMY SCHOOL
MONTGOMERY COUNTY

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2001

Increase (Decrease) in Cash and Cash Equivalents:	
Cash Flows from Operating Activities:	
Cash Received from State of Ohio Government	$ 4,212,920
Cash Payments for Employee Benefits	(105,564)
Cash Payments to Suppliers for Goods and Services	(3,991,583)
Net Cash Provided By Operating Activities	115,773
Cash Flows from Noncapital Financing Activities:	
Federal, and State Grants Received	92,347
Cash Flows from Capital and Related Financing Activities:	
Cash Received from Sale of Fixed Assets	169,579
Cash Flows from Noncapital Investing Activities:	
Interest Income	48,028
Private Grants	57,396
Net Cash Provided for Noncapital Financing Activities	105,424
Net Increase in Cash and Cash Equivalents	483,123
Cash and Cash Equivalents at Beginning of Year	293,889
Cash and Cash Equivalents at End of Year	777,012
Reconciliation of Operating Loss to Net Cash Provided By Operating Activities:	
Operating Loss	(457,282)
Adjustments to Reconcile Operating Loss to Net Cash Provided By Operating Activities:	
Depreciation and amortization	3,816
Change in Assets and Liabilities:	
Decrease in Other Receivable	340,298
Increase in Intergovernmental Receivable	(42,339)
Decrease in Accounts Payable	(64,296)
Increase in Accrued Edison Fees	335,576
Net Cash Provided By Operating Activities	$ 115,773

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

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1. DESCRIPTION OF THE SCHOOL AND REPORTING ENTITY

Alliance Community Schools, Inc. "Doing Business As" Dayton Academy School (the School) is a nonprofit corporation established pursuant to Ohio Rev. Code Chapters 3314 and 1702 to maintain and provide a school exclusively for any educational, literary, scientific and related teaching service. Specifically, the School's purpose is to be a charter school serving children from kindergarten through grade five during its first year and adding a grade over the next three years, extending through grade eight by the 2003 school year. The School, which is part of the state's education program, is to operate or arrange for the operation of schools in the Dayton, Ohio area. 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 qualifies as an exempt organization 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 school's tax-exempt status.

The creation of the School was initially proposed to the Ohio State Board of Education, the sponsor, by the Board of Trustees of Alliance Community Schools, Inc. (the Board) on November 9, 1998. The Ohio State Board of Education approved the proposal and entered into a contract with the Board, which provided for the commencement of School operations beginning the fiscal year 2000 academic year and shall terminate upon conclusion of the fiscal year 2004 school year.

The School operates under a seven member Board of Trustees. This Board exercises its authority by appointing a separate five member Board of Governance for the School. The Board of Trustees 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 qualifications of teachers. The Board of Governance controls the School's one instructional facility staffed by 39 teaching personnel who provide services to approximately 624 students. Furthermore, Dayton Academy School and Dayton View Academy School share the same Board. (See note 8C.)

The primary government of the School consists of one fund, several departments, and the boards and committees that are not legally separate from the School. This includes general operations and student related activities of the School.

Alliance Community Schools has several divisions. These divisions operate under the names of Dayton Academy and Dayton View Academy. The School also leases its facilities from a separately Incorporated Ohio Not-for-Profit entity Alliance Facilities Management (AFM). (See note 8A.) Alliance Community Schools Inc. has contracted with Edison Schools, Inc. to act as a management company for both of the Schools. (See Note 12.) In addition, the secretary of Alliance Community Schools, Inc. was also employed as the School's legal counsel. (See note 8B.) Likewise, the accounting firm employed to perform the School's conversion to generally accepted accounting principals (GAAP), also performed the duties fiscal officer for the School. (See note 8D.)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the School have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental nonprofit organizations. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The School also applies Financial Accounting Standards Board (FASB) statements and interpretations issued on or before November 30, 1989, provided they do not conflict with or contradict GASB pronouncements. The more significant of the School's accounting policies are described below:

A. Basis of Presentation

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

B. 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 and all liabilities are included on the balance sheet. Operating statements present increases (e.g. revenues) and decreases (e.g. expenses) in net total assets.

Basis of accounting refers to when revenues and expenses are recognized in the accounts and reported in the financial statements. Basis of accounting relates to the timing of the measurements made.

The accrual basis of accounting is used for reporting purposes. Under this basis, revenues are recognized when they are earned, and expenses are recognized when they are incurred.

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 the Ohio Revised Code Chapter 5705, unless specifically provided by the School's contract with its sponsor. The contract between Alliance Community Schools, Inc. and it's sponsor, Ohio State Board of Education, requires a detailed school budget for each year of the School's contract, however, the budget is not required to follow the provisions of Ohio Rev. Code Section 5705.

D. Cash and Cash Equivalents

The School's fiscal officer accounts for all monies received by the School. To improve cash management, all cash received from the State of Ohio is electronically transferred into the main checking account. This checking account is set up as a sweep account. Individual fund integrity is maintained through School records and the accounting system.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

E. Estimates

The preparation of the financial statements in conformity with general accepted accounting principles (GAAP), requires management to make certain 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 $1,000. The School does not possess any infrastructure. The School did not capitalize any interest during the period. 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. The School sold the remainder of the fixed assets they owned to their management company, Edison Schools, Inc., during the fiscal year. The management company now owns all assets related to the School, with exception to the school building which is owned by a related organization, Alliance Facilities Management. (See note 8A.)

G. Intergovernmental Revenue

The School currently participates in the State Foundation Program and the State Disadvantaged Pupil Impact Aid (DPIA) Program. Revenues received from these programs are recognized as operating revenues in the accounting period in which all eligibility requirements have been met.

Grants and entitlements are recognized as non-operating revenues in the accounting period in which all eligibility requirements have been met.

Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted, matching requirements, in which the School must provide local resources to be used for a specified purpose, and expenditure requirements, in which the resources are provided to the School on a reimbursement basis.

The School also participates in various federal and state programs through the Ohio Department of Education. The programs the School participated in during fiscal year 2000, of which they were still owed for at June 30, 2001 include: Title I, Title II, Title IV, Title VI, and, Title VI-R. The School did not apply for any federal grants for fiscal year 2001. Revenue to be received from these programs is recognized as non-operating revenue in the accompanying financial statements.

Amounts owed to the School under the above named programs for the 2000 school year totaled $309,459 at June 30, 2001, and is reflected on the accompanying financial statements as an intergovernmental receivable.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

H. Compensated Absences

The School's contract with Edison Schools, Inc. states Edison will process all payroll and employees will follow Edison's personnel policies. This policy also states that any unused sick leave does not carryover to successive years, and there is no payment of sick leave upon separation. In addition, the abovementioned policy states all vacation should be taken within the year it is earned. Therefore, neither sick nor vacation leave is accrued as a liability.

3. DEPOSITS AND INVESTMENTS

The funds for Dayton View Academy and Dayton Academy were pooled into one bank account. During October 2001, separate accounts were established for each School. At year end, the combined bank balance of these Schools' deposits and investments was $1,625,324, of which $777,012 was allocated to Dayton Academy.

The following information classifies deposits and investments by categories of risk as defined in GASB Statement No. 3, Deposits with Financial Institutions, Investments (including Repurchase Agreements), and Reverse Repurchase Agreements.

Deposits: At year-end the carrying amount of the School's deposits was $10,000 and the bank balance was $770,012. Of the bank balance:

a. $10,000 was covered by federal deposit insurance.

b. $767,012 was uninsured and uncollateralized. Although all statutory requirements for the deposit of money had been followed, noncompliance with federal requirements could potentially subject the School held to a successful claim by the FDIC.

Investments: The School's investments are required to be categorized to give an indication of the level of risk assumed by the School at year end. Category 1 includes investments that are insured or registered or for which the securities are held by the School or its agent in the School's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the School's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in the School's name.

3. DEPOSITS AND INVESTMENTS (Continued)

	Category of Risk 3	Fair Value
Overnight Repurchase Agreement	$767,012	$767,012

The classification of cash in pooled cash, cash equivalents on the balance sheet is based on criteria set forth in GASB Statement No. 9.

A reconciliation between the classifications of cash in pooled cash, cash equivalents, on the balance sheet per GASB Statement No. 9 and the classifications of deposits and investments presented above per GASB Statement No. 3 is as follows:

	Pooled Cash and Cash Equivalents	Investments
GASB Statement No. 9	$ 777,012	
Investments of the Cash Management Pool:		
Overnight Repurchase Agreement	(767,012)	767,012
GASB Statement No. 3	$ 10,000	$767,012

4. RECEIVABLES

Receivables at June 30, 2001 consisted of intergovernmental (State foundation and federal grant) receivables and other 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. Other receivables is $13,601 due from Alliance Facilities Management, Inc., for overpayment of rent. (See note 8A.)

A summary of the principal items of receivables is as follows:

Intergovernmental Receivable:		
State Foundation	$	98,778
Title I		177,808
Title II		3,563
Title IV		4,383
Title VI		3,153
Title VI-R		21,774
Total Intergovernmental Receivable	$	309,459

In November 2000, the School forgave a $133,644 receivable from Alliance Facilities Management, Inc. (AFM).

5. RISK MANAGEMENT

A. Property and Liability

The School is exposed to various risks of loss related to torts, theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During the year ended 2001, the School's management company, Edison Schools, Inc., carried comprehensive insurance on all of the schools they manage. This policy cannot be broken out on a per school basis, and therefore is presented on a cumulative basis. Edison Schools, Inc. contracted with Willis of Tennessee, Inc. for employee dishonesty (crime and fiduciary) bonds, business personal property, equipment hardware and software, general liability, and excess liability insurance.

Employee dishonesty crime coverage carries a $10,000 deductible and has a $1,000,000 limit. Employee dishonesty fiduciary liability also has a limit of $1,000,000, with no deductible. Computer equipment carries a $10,000 deductible and has a $30,000,000 limit. Business personal property has a limit of $32,500,000, with a $10,000 deductible. General liability coverage provides $1,000,000 per occurrence and $2,000,000 in the aggregate. In addition, the general liability provides $100,000 for fire damage for any one fire, and $5,000 for medical expenses for any one person.

B. Employee Medical, Dental and Vision Benefits

As part of the management agreement with Edison Schools, Inc. (See note 12B.), insurance benefits for School employees are paid by Edison.

6. STATE SCHOOL FUNDING DECISION

On September 6, 2001, the Ohio Supreme Court issued its latest opinion regarding the State's school funding plan. The decision identified aspects of the current plan that require modification if the plan is to be considered constitutional, including:

- A change in the school districts that are used as the basis for determining the base cost support amount. Any change in the amount of funds distributed to school districts as a result of this change must be retroactive to July 1, 2001, although a time line for distribution is not specified.

- Fully funding parity aid no later than the beginning of fiscal year 2004 rather than fiscal year 2006.

The Supreme Court relinquished jurisdiction over the case based on anticipated compliance with its order.

In general, it is expected that the decision would result in an increase in State funding for most Ohio school districts. However, as of February 29, 2002, the Ohio General Assembly is still analyzing the impact this Supreme Court decision will have on funding for individual school districts. Further, the State of Ohio, in a motion filed September 17,2001, asked the Court to reconsider and clarify the parts of the decision changing the school districts that are used as the basis for determining the base cost support amount and the requirement that changes be made retroactive to July 1, 2001.

6. STATE SCHOOL FUNDING DECISION (Continued)

On November 2, 2001, the Court granted this motion for reconsideration. The Court may re-examine and redetermine any issue upon such reconsideration.

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

7. CONTINGENCIES

A. Grants

The School received financial assistance from federal and state agencies in the form of grants. The disbursement of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and is subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the School. However, in the opinion of management, any such disallowed claims will not have a material adverse effect on the overall financial position of the School at June 30, 2001.

B. Pending 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. The effect of this suit, if any, on the School is not presently determinable.

C. State Funding

The Ohio Department of Education conducts reviews of enrollment data and 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. During the fiscal year ended June 30, 2000, the School billed the state of Ohio in excess of the amounts due to them based on an estimated number of pupils the School expected the first year. The amount outstanding at June 30, 2001 was $247,971 and is reported as an intergovernmental payable. The School is to repay the state of Ohio with monthly deductions from FYE 2002 foundation payments which are scheduled to begin in October 2001 and end in June 2002.

During the fiscal year ended June 30, 2001, the School billed the state of Ohio less than the amounts due to them based on an estimated number of pupils the School expected for the year. The amount due at June 30, 2001 was $98,778 and is reported as an intergovernmental receivable. (See note 4.) The State of Ohio has estimated repayment to the School during the February 2002 foundation payments.

7. CONTINGENCIES (Continued)

D. Accountability

The School is required to disclose all instances of violations of finance related legal provisions. During the audit period the School was found to be in violation of the following provision:

Ohio Rev. Code Section 3314.08(J) states a community school may borrow money to pay any necessary and actual expenses of the school in anticipation of the receipt of any portion of the payment to be received by the school pursuant to division (D) of the section. The school may issue notes to evidence such borrowing to mature no later than the end of the fiscal year in which such money is borrowed. The proceeds of the notes shall be used only for the purposes for which the anticipated receipts may be lawfully expended by the school. The School issued a long-term note to Edison, the School's management company, which matures on June 15, 2008.

8. RELATED PARTY TRANSACTIONS

A. Alliance Facilities Management (AFM)

The School leases its facilities and land from Alliance Facilities Management (AFM), which is also created under Alliance Community Schools, Inc. The lease expense for the year ended June 30, 2001 was $395,388 for the facilities and $60,589 for the land. (See note 9.)

B. Secretary of Alliance Community Schools, Inc

The Secretary of Alliance Community Schools, Inc. was also employed as the School's attorney. Total payments made for related legal fees during the year ended June 30, 2001 was $112,626. The School also had a payable to the firm at June 30, 2001 in the amount of $1,341.

C. Board of Governance

Although no transactions occurred between Dayton View Academy and Dayton Academy, both schools share the same Board of Governance.

D. Accounting Firm and Fiscal Officer

The School employed an accounting firm to perform their GAAP conversion. In addition, the accounting firm performed the duties of fiscal officer for the School. Total payments made for related accounting services during the year ended June 30, 2001 was $30,833.

9. LEASES

The School subleases a building and 4.441 acres together with the non-exclusive right to use and occupy some common areas through a related nonprofit organization, Alliance Facilities Management (AFM). (See note 8A.) AFM leases the land from the Young Men's Christian Association (YMCA). The School agreed to pay AFM, as rent for the land and the common areas, an amount equal to the land lease due by AFM owed to the YMCA. Rent paid for the land for the year ended June 30, 2001 was $60,589.

The above mentioned lease also states the School must pay AFM for rent of the building, an amount equal to the debt service relating to any financing obtained; plus loan closing cost, on going loan administration cost associated with any financing secured by the premises, including but not limited to, cost associated with satisfying the financial reporting and periodic appraisal requirements; plus out of pocket expenses incurred by AFM; plus $5,000 per year. The School, with written notification, has an option to renew the lease for four additional terms of five years. Rent paid for the building for the year ended June 30, 2001 was $395,388.

The estimated future minimum lease payments as of June 30, 2001, is as follows:

Year Ending June 30,	Land Minimum Lease Payments	Building Minimum Lease Payments	Total Minimum Lease Payments
2002	$ 73,440	$ 435,888	$ 509,328
2003	84,000	435,888	519,888
2004	86,520	435,888	522,408
2005	89,040	435,888	524,928
	$ 333,000	$ 1,743,552	$ 2,076,552

10. PURCHASED SERVICES

For the period July 1, 2000 through June 30, 2001, purchased services expenses were payments for services rendered by various vendors as follows:

Management Company Fees	$3,734,378
Food Service (On-Behalf of Expenditures)	240,100
Total	$3,974,478

11. MANAGEMENT FEES CONVERTED TO PROMISSORY NOTE

The School had accrued Edison Fees at June 30, 2000, of which $500,000 was converted to a promissory note, at 10% interest, on January 21, 2001. The balance of the note at June 30, 2001 was $460,768. Payments made to the management company, Edison Schools, Inc. liquidate this note, and therefore no principal or interest payments are reflected on the financial statements. A citation was issued due to this action being in violation of Ohio Revised Code section 3314.08(J) which states a community school cannot repay debt, for a period longer than one year with state funds.

11. MANAGEMENT FEES CONVERTED TO PROMISSORY NOTE (Continued)

During fiscal year 2001 the School's payments for the promissory note include $39,232 in principal and $44,226 in interest. The following is a summary of the School's future annual debt service requirements to maturity for its long-term note payable:

Year Ending June 30	Principal	Interest	Total
2002	$51,227	$ 43,565	$ 94,792
2003	52,452	38,593	91,045
2004	57,944	33,101	91,045
2005	64,012	27,033	91,045
2006	70,714	20,331	91,045
2007 - 2008	164,419	17,761	182,180
Total	$460,768	$180,384	$641,152

12. AGREEMENT WITH EDISON SCHOOLS, INC.

On May 23, 2000, the School contracted with Edison Schools Inc, to provide educational programs that offer educational excellence and a laboratory for educational innovation based on Edison's unique school design, comprehensive educational programs, and management principles. The term of the contract is retroactive to August 1, 1999 and ending on June 30, 2004. The contract shall be renewed for an additional five year term, up to a total of two additional five year terms and cannot extend beyond the term of the School's contract with the Ohio State Board of Education. Under the contract Edison is responsible and accountable to Alliance Community School's Inc. Board of Trustees for the administration, operation, and performance of the School in accordance with the School's contract with the Ohio State Board of Education to operate the School. Significant provisions of the contract are as follows:

A. Financial Provisions

1. Management Consulting and Operation Fee

The School is required to remit monthly to Edison all qualified gross revenue defined in the contract as "Appendix F" except for $75,000 and rent and common area rental. In addition, the School shall pay to Edison fees of $40,000 and $55,000 for the 2000 - 2001 school year, as stated in Article 8 of the contract.

The following is a summary of current payment activity to Edison:

Amount due current fiscal year	$3,780,319
Amount remitted current fiscal year	(3,384,065)
Accrued Edison Fees	$396,254

2. The School's Financial Responsibilities

The School is responsible for initial start up costs, rent and common area rental, and the Promissory Note. (See note 11.) The School is also responsible to pay for fees for audit and legal services not related to the operation of the School.

12. AGREEMENT WITH EDISON SCHOOLS, INC. (Continued)

3. Edison Financial Responsibilities

Edison is responsible for costs associated with operating the School. Such costs shall include, but shall not be limited to, salaries and benefits, including payroll taxes; pension and retirement; the purchase of curriculum materials, textbooks, computers and other equipment, software, and supplies; insurance premiums, utilities, janitorial services, legal and financial management services related to the operation of the School and repairs and maintenance of the School's facilities, except for capital repair. Edison shall equip the School's facilities with desks and other furniture and furnishings and these items are considered property of Edison.

Edison must secure and maintain commercial general liability coverage for bodily injury and property damage; Educator Liability coverage; Automobile Liability insurance, for personal injury and property damage; Property Insurance for facilities; and Workers Compensation insurance for employees. (See note 5A.)

4. Budget

Edison shall provide the School with an annual budget, in reasonable detail, by the 30th of June of each year.

B. Personnel

All personnel working at the School are employees of the Alliance Community Schools, Inc. except the Business Service Manger, who is an employee of Edison. Edison shall have the responsibility to select, assign, evaluate, and discharge School employees. Compensation will be set according to Edison's compensation policies for Teachers, Principals, and Non-Instructional Staff.

In addition, any accrued payroll, the related benefits, and pension obligation for the School's employees are included in the Accrued Edison Fees, as these amounts are included in the amount of revenues remitted to Edison throughout the school year.

C. Agreement Termination

1. Termination by the School

The School may terminate the Contract in the event Edison materially breaches the Contract and Edison fails to remedy such breach within 60 days of its receipt of written notice of such breach from the School.

2. Termination by Edison

Edison may terminate the Contract in the event the School materially breaches the Contract and the School fails to remedy such breach within 60 days of its receipt of written notice of such breach from Edison.

13. FOOD SERVICE AGREEMENT

Dayton Academy (the School) contracted with Dayton City School District (the District) to facilitate their food service operations. The District's food service employees provide breakfast, and lunch to children at Dayton Academy. The District sets the food prices, processes all free and reduced meal applications, and handles all food service money. The students at Dayton Academy that are eligible for free or reduced meals are therefore included in Dayton City School District's federal grant application. The money the District receives on-behalf-of the School is recorded as federal and state grants on the School's financial statements. (See note 10.)

14. SUBSEQUENT EVENTS

On November 19, 2001, the School applied for and subsequently received a $250,000 grant from the Ohio Department of Education. This transaction is not recognized in the financial statements.

15. DEFINED BENEFIT PENSION PLANS

A. School Employees Retirement System

The School contributes to the School Employees Retirement System of Ohio (SERS), a cost-sharing multiple employer 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 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, 45 N. Fourth Street, Columbus, Ohio 43215-3634.

Plan members are required to contribute 9 percent of their annual covered salary and the School is required to contribute at an actuarially determined rate. The current 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 2001, 4.2 percent of annual covered salary was the portion used to fund pension obligations.

For fiscal year 2000, 5.5 percent was 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, 2001 and 2000, were $17,325 and $31,776, respectively; 100 percent has been contributed for fiscal year 2001 and 100 percent for fiscal year 2000.

B. State Teachers Retirement System

The School contributes to the State Teachers Retirement System of Ohio (STRS), a cost-sharing multiple employer public employee retirement system. STRS provides retirement and disability benefits, annual cost-of-living adjustments, and death and survivor benefits to members and beneficiaries. Benefits are established by Chapter 3307 of the Ohio Revised Code. STRS issues a publicly available, stand-alone financial report that includes financial statements and required supplementary information for STRS. That report may be obtained by writing to the State Teachers Retirement System, 275 East Broad Street, Columbus, Ohio 43215-3371.

15. DEFINED BENEFIT PENSION PLANS (Continued)

For the fiscal year ended June 30, 2001, plan members were required to contribute 9.3 percent of their annual covered salaries. The School was required to contribute 14 percent; 9.5 percent was the portion used to fund pension obligations. For fiscal year 2000, the portion used to fund pension obligations was 6.0 percent. Contribution rates are established by STRS, upon recommendations of its consulting actuary, not to exceed statutory maximum rates of 10 percent for members and 14 percent for employers. The School's required contributions for pension obligations to STRS for the fiscal years ended June 30, 2001 and 2000 were $135,066 and $76,485, respectively; 100 percent has been contributed for fiscal year 2001 and 100 percent for fiscal year 2000.

As described in Note 12B the school is responsible for all personnel matters. As also described in Note 12B, the school has an agreement with Edison Schools Inc. that all transactions related to School personnel are handled by Edison throughout the year, funding for which is included in the revenues remitted to Edison. All accrued payroll, related benefits and pension obligations are to be paid by Edison Schools Inc. Management has no reason to believe, as of the date of this report, the School has any additional liability for any of these obligations.

16. POSTEMPLOYMENT BENEFITS

The School provides comprehensive health care benefits to retired teachers and their dependents through the State Teachers Retirement System (STRS), and to retired non-certified employees and their dependents through the School Employees Retirement System (SERS). Benefits include hospitalization, physicians' fees, prescription drugs and reimbursement of monthly Medicare premiums. Benefit provisions and the obligations to contribute are established by the Systems based on authority granted by State statute. Both systems are on a pay-as-you-go basis.

All STRS benefit recipients and sponsored dependents are eligible for health care coverage. The STRS Board has statutory authority over how much, if any, of the health care costs will be absorbed by STRS. Most benefit recipients pay a portion of the health care cost in the form of a monthly premium. By law, the cost of coverage paid from STRS funds is included in the employer contribution rate, currently 14 percent of covered payroll. For the fiscal year ended June 30, 2001, the STRS Board allocated employer contributions equal to 4.5 percent of covered payroll to the Health Care Reserve Fund. For the School District, this amount equaled $63,978 for fiscal year 2001.

STRS pays health care benefits from the Health Care Reserve Fund. At June 30, 2000, (the latest information available) the balance in the Fund was $3,419 million. For the year ended June 30, 2000, net health care costs paid by STRS were $283,137,000 and STRS had 99,011 eligible benefit recipients.

For SERS, coverage is made available to service retirees with ten or more fiscal years of qualifying service credit, and to 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.

16. POSTEMPLOYMENT BENEFITS (Continued)

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, 2001, employer contributions to fund health care benefits were 9.80 percent of covered payroll, an increase of 1.3 percent from fiscal year 2000. 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 2001, the minimum pay was established at $12,400. For the School, the amount contributed to fund health care benefits, including the surcharge, during the 2001 fiscal year equaled $40,426. 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 the annual health care expenses. Expenses for health care for the fiscal year ended June 30, 2000 (the latest information available), were $140,696,340 and the target level was $211 million. At June 30, 2000, SERS had net assets available for payment of health care benefits of $252.3 million. SERS has approximately 50,000 participants currently receiving health care benefits.

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

Dayton Academy School
Montgomery County
4401 Dayton-Liberty Rd.
Dayton, Ohio 45418

To the Board of Governance:

We have audited the financial statements of Dayton Academy School (the School), Montgomery County, as of and for the year ended June 30,2001, and have issued our report thereon dated February 29, 2002. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the School's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under *Government Auditing Standards* which is described in the accompanying schedule of findings as item 2001-10357-001. We also noted certain immaterial instances of noncompliance that we have reported to management of the School in a separate letter dated February 29, 2002.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the School's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the School's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of findings as items 2001-10357-002 and 2001-10357-003.

**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, we believe none of the reportable conditions described above are material weaknesses. We also noted other matters involving the internal control over financial reporting that do not require inclusion in this report, that we have reported to management of the School in a separate letter dated February 29, 2002.

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

Jim Petro
Auditor of State

February 29, 2002

DAYTON ACADEMY SCHOOL
MONTGOMERY COUNTY

SCHEDULE OF FINDINGS
JUNE 30, 2001

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

FINDING NUMBER 2001-10357-001

Ohio Rev. Code Section 3314.08(J) states a community school may borrow money to pay any necessary and actual expenses of the school in anticipation of the receipt of any portion of the payment to be received by the school pursuant to division (D) of the Section. The school may issue notes to evidence such borrowing to mature no later than the end of the fiscal year in which such money is borrowed. The proceeds of the notes shall be used only for the purposes for which the anticipated receipts may be lawfully expended by the school. The School issued a long-term note to Edison Schools Inc, the School's management company, which matures on June 15, 2008. To comply with the abovementioned Section of Code, the Board should determine a method to effectively eliminate this note.

FINDING NUMBER 2001-10357-002

Dayton Academy School and Dayton View Academy School are separate schools created under the same company, Alliance Community Schools, Inc. However, these two schools shared the same bank account during fiscal year 2001. In addition, one check was often written for both schools invoices that were to the same vendor. The School's established separate bank accounts during October 2001, but had their finances combined throughout the entire fiscal year, and had to separate the transactions after year end. For proper accountability of each schools financial activity, the School's should maintain separate bank accounts and a separate financial records.

FINDING NUMBER 2001-10357-003

Certain deficiencies were noted in the School's procedures for payment of legal fees. For verification of accuracy of legal fee payments, the School should address the following conditions.

- There was no Governing Board (the Board) approved contract or agreement between the Board and the law firm. A Board approved contract or agreement, as to the services that will be rendered, could avoid the School paying for legal services the School did not request. For proper accountability and control of the payment of legal fees, the Treasurer and the Board should closely monitor legal fees and enter into a contract or agreement, with the law firm, as to the services that will be rendered.

- The School paid $112,626 of legal fees during the fiscal year, of which $58,425 included payments of another entity's legal fees (Alliance Facilities Management Inc.). An invoice for Alliance Facilities Management, Inc., a separate not-for-profit, was submitted and paid by the School. Alliance Facilities Management Inc. repaid $44,886, the remaining balance owed was $13,539. The Treasurer and Board should closely monitor invoices paid to ensure all invoices paid are for the School.

Subsequently an amount was paid toward the $58,425 and $13,539 is included as an other receivable on the financial statements.

DAYTON ACADEMY SCHOOL
MONTGOMERY COUNTY

SCHEDULE OF PRIOR AUDIT FINDINGS
JUNE 30, 2001

Finding Number	Finding Summary	Fully Corrected?	Not Corrected, Partially Corrected; Significantly Different Corrective Action Taken; or Finding No Longer Valid; ***Explain***:
2000-10357-001	Ohio Rev. Code Sections 3309.47 and 3309.49 - Delinquent SERS payments.	Yes	Fully corrected during fiscal year 2001.
2000-10357-002	Ohio Rev. Code Section 3314.03(A)(11)(g) - Failure to submit annual report of activities.	Yes	Fully corrected during fiscal year 2001.

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DAYTON ACADEMY 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
MAY 9, 2002