TOLEDO SCHOOL FOR THE ARTS
LUCAS COUNTY

SINGLE AUDIT

FOR THE YEAR ENDED JUNE 30, 2002

Auditor of State
Betty Montgomery

TOLEDO SCHOOL FOR THE ARTS

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Auditor of State
Betty Montgomery

INDEPENDENT ACCOUNTANTS' REPORT

Toledo School for the Arts
Lucas County
425 Jefferson Avenue
Toledo, OH 43604-1060

To the Governing Board:

We have audited the Balance Sheet of the Toledo School for the Arts, Lucas County, (the School) as of June 30, 2002, and the related Statement of Revenues, Expenses, and Changes in Accumulated Deficit, and the Statement of Cash Flows for the year ended June 30, 2002. These financial statements are the responsibility of the School's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the School as of June 30, 2002, and the results of operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming the School will continue as a going concern. As shown in the financial statements, the School has incurred an operating loss in the amount of $370,795 for the year ended June 30, 2002, has a working capital deficiency of $465,544 as of June 30, 2002, an accumulated deficit of $256,833, and has been unable to pay it's obligations when due. Accordingly, there is substantial doubt about the School's ability to continue as a going concern. Management's plans in regards to these matters are discussed in Note 18. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

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In accordance with *Government Auditing Standards*, we have also issued our report dated May 1, 2003, on our consideration of the School's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The accompanying schedule of federal awards expenditures is presented for additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements. We subjected this information to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

Betty Montgomery

Betty Montgomery
Auditor of State

May 1, 2003

TOLEDO SCHOOL FOR THE ARTS

BALANCE SHEET
AS OF JUNE 30, 2002

Assets	
Current Assets	
Cash and Cash Equivalents with Fiscal Agent	$18,486
Accounts Receivable	7,269
Intergovernmental Receivables	20,655
Prepaid Items	638
Total Current Assets	47,048
Non-Current Assets	
Security Deposit	13,903
Fixed Assets (Net of Accumulated Depreciation)	295,008
Total Assets	$355,959
Liabilities and Equity	
Current Liabilities	
Accounts Payable	$85,209
Accrued Wages	88,281
Intergovernmental Payable	79,165
Due to Students	1,992
Accrued Interest Payable	1,429
Notes Payable - Current Portion	248,353
Capital Leases Payable	8,163
Total Current Liabilities	512,592
Long-Term Liabilities	
Capital Leases Payable	12,276
Total Liabilities	524,868
Equity	
Contributed Capital	87,924
Accumulated Deficit	(256,833)
Total Liabilities and Equity	$355,959

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

TOLEDO SCHOOL FOR THE ARTS

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN ACCUMULATED DEFICIT FOR THE YEAR ENDED JUNE 30, 2002

Operating Revenues	
Foundation Payments	$1,045,003
Disadvantaged Public Impact Aid	$22,555
Food Services	3,206
Classroom Materials and Fees	15,088
Other Operating Revenues	262
Total Operating Revenues	1,086,114
Operating Expenses	
Salaries	797,607
Fringe Benefits	145,167
Purchased Services	286,849
Materials and Supplies	59,473
Depreciation	117,369
Other Operating Expenses	50,444
Total Operating Expenses	1,456,909
Operating (Loss)	(370,795)
Non-Operating Revenues (Expenses)	
Grants Received - State	7,675
Grants Received - Federal	322,498
Contributions and Donations	120,487
Interest Earnings	1,081
Interest and Fiscal Charges	(9,815)
Miscellaneous Non-Operating Revenue	7,205
Total Non-Operating Revenues (Expenses)	449,131
Net Income	78,336
Accumulated Deficit at Beginning of Year	(335,169)
Accumulated Deficit at End of Year	($256,833)

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

TOLEDO SCHOOL FOR THE ARTS

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

Increase (Decrease) in Cash and Cash Equivalents	
Cash Flows from Operating Activities	
Cash Received from State Foundation	$990,280
Cash Received from Disadvantaged Pupil Impact Aid	22,555
Cash Received from Food Services	3,206
Cash Received from Classroom Materials and Fees	16,192
Cash Received from Other Operating Sources	822
Cash Payments to Suppliers for Goods and Services	(427,467)
Cash Payments to Employees for Services	(794,646)
Cash Payments for Employee Benefits	(152,087)
Cash Payments for Other Operating Uses	(44,220)
Net Cash Used for Operating Activities	(385,365)
Cash Flows from Noncapital Financing Activities	
Proceeds from Issuing Debt	56,667
Grants Received - State	7,675
Grants Received - Federal	325,535
Miscellaneous Non-Operating Revenue	8,759
Contributions and Donations	114,078
Principal Payments	(14,489)
Interest Payments	(11,401)
Net Cash Provided by Noncapital Financing Activities	486,824
Cash Flows from Capital and Related Financing Activities	
Payments for Capital Acquisitions	(114,266)
Principal Payments	(5,825)
Interest Payments	(741)
Net Cash Used for Capital and Related Financing Activities	(120,832)
Cash Flows from Investing Activities	
Cash Received from Interest on Investments	1,081
Net Cash Provided by Investing Activities	1,081
Net Decrease in Cash and Cash Equivalents	(18,292)
Cash and Cash Equivalents at the Beginning of the Year	36,778
Cash and Cash Equivalents at the End of the Year	$18,486

(Continued)

TOLEDO SCHOOL FOR THE ARTS

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

Reconciliation of Operating Loss to	
<u>Net Cash Used for Operating Activities</u>	
Operating Loss	($370,795)
Adjustments to Reconcile Operating Loss to	
<u>Net Cash Used for Operating Activities</u>	
Depreciation	117,369
Changes in Assets and Liabilities:	
(Increase) in Accounts Receivable	(6,122)
(Increase) in Prepaid Items	(105)
(Decrease) in Accounts Payable	(96,491)
Increase in Accrued Wages Payable	31,158
(Decrease) in Compensated Absences Payable	(2,391)
(Decrease) in Intergovernmental Payable	(50,138)
(Decrease) in Capital Lease Payable	(7,850)
Total Adjustments	(14,570)
Net Cash Used for Operating Activities	($385,365)

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

1. DESCRIPTION OF THE SCHOOL AND REPORTING ENTITY

Toledo School for the Arts (the School) is a nonprofit corporation established pursuant to Ohio Revised Code Chapters 3314 and 1702. The School is an approved tax-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 School's objective is to provide students the opportunity to achieve personal and academic success through arts-based learning. The School's programs are currently available to students in grades 7 - 11, but will be adding the 12th grade in the 2003 school year. The School, which is part of the State's education program, is independent of any school district and is nonsectarian in its programs, admission policies, employment practices, and all other operations. The School may acquire facilities as needed and contract for any services necessary for the operation of the school.

The School was approved for operation under a contract with the Toledo City School District (the Sponsor) for a period of five years commencing June 22, 1998, with operations starting in July of 1999. The Sponsor is responsible for evaluating the performance of the School and has the authority to deny renewal of the contract at its expiration or terminate the contract prior to its expiration. The School entered into a separate agreement with the Treasurer of Lucas County Educational Service Center to serve as the Chief Financial Officer of the School (See Note 13).

The School operates under the direction of a twenty member Governing Board. The Governing 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 qualifications of teachers. The Governing Board controls the School's one instructional/support facility staffed by 5 non-certified personnel and 41 certificated teaching personnel who provide services to 268 students.

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/or net income is appropriate for capital maintenance, public policy, management control, accountability or other purposes.

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. Equity (i.e., net total assets) is segregated into contributed capital and accumulated deficit components.

Operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total assets.

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

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

C. Budgetary Process

Unlike other public schools located in the state of Ohio, community schools are not required to follow budgetary provisions set forth in Ohio Revised Code Chapter 5705, unless specifically provided in the School's contract with its Sponsor. The contract between the School and its Sponsor does prescribe an annual budget requirement in addition to preparing a 5-year forecast which is to be updated on an annual basis.

D. Cash and Cash Equivalents

All monies received by the School are accounted for by the School's fiscal agent, the Lucas County Educational Service Center. All cash received by the fiscal agent is maintained in separate bank accounts in the School's name. Monies for the School are maintained in these accounts or temporarily used to purchase short-term investments.

For the purposes of the statement of cash flows and for presentation on the balance sheet, investments with original maturities of three months or less at the time they are purchased by the School are considered to be cash equivalents.

E. Fixed Assets and Depreciation

Fixed assets are capitalized at cost and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market value as of the dates received. The School does not possess any infrastructure.

Improvements are capitalized. The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset's life are not capitalized.

Depreciation of furniture, equipment, and leasehold improvements is computed using the straight-line method over an estimated useful life of five years. Improvements to fixed assets are depreciated over the remaining useful lives of the related fixed assets.

F. Intergovernmental Revenues

The School currently participates in the State Foundation Program, the State Disadvantaged Pupil Impact Aid (DPIA) Program, and the State Special Education Program. Revenues 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 the Federal Charter School Grant Program through the Ohio Department of Education. Under this program, the School was awarded $300,000 to offset costs of the School. Revenue received from this program is recognized as non-operating revenue in the accompanying financial statements.

Amounts awarded under the above named programs for the 2002 school year totaled $1,397,731.

G. Prepaid Items

Payments made to vendors for services that will benefit periods beyond June 30, 2002, are recorded as prepaid items using the consumption method by recording a current asset for the prepaid amount and reflecting the expense in the year in which services are consumed.

H. Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

I. Contributed Capital

Contributed capital represents equity obtained from private sources provided to the School that are not subject to repayment. These assets are recorded at their fair market value on the date contributed. Depreciation on those assets acquired with contributed resources is expensed. There were no additions to contributed capital in fiscal year 2002.

J. Compensated Absences

Vacation benefits are accrued as a liability as the benefits are earned if the employees' rights to receive compensation are attributable to services already rendered and it is probable that the School will compensate the employees for the benefits through paid time off or some other means. The School records a liability for accumulated unused vacation time when earned for all employees. There was no accrued vacation in fiscal year ended 2002.

K. Security Deposit

The School entered into a lease for the use of a building for the operation of the School. Based on the lease agreement, a security deposit was required to be paid at the signing of the agreement. This amount is held by the lessor.

3. ACCOUNTABILITY AND COMPLIANCE

Accumulated Deficit and Operating Loss

The School is analyzing operations and admissions procedures to determine appropriate steps to alleviate the deficit and operating losses (See Note 18).

4. DEPOSITS AND INVESTMENTS

At June 30, 2002, the carrying amount of the School's deposits was $18,486 and the bank balance was $52,966. The bank balance was covered by federal depository insurance.

5. RECEIVABLES

Receivables at June 30, 2002, consisted of accounts receivable and intergovernmental (e.g., grants) receivables. Accounts receivable consists of a miscellaneous type of receipt and is collectible in full due to the unique nature of the receivable. All intergovernmental receivables are considered collectible in full, due to the stable condition of State programs, and the current year guarantee of federal funds.

6. FIXED ASSETS

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

Leasehold Improvements	$380,370
Furniture and Equipment	206,475
Subtotal	586,845
Less: Accumulated Depreciation	(291,837)
Net Fixed Assets	$295,008

7. RISK MANAGEMENT

A. Property and Liability

The School is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. For fiscal year 2002, the School had the following insurance coverage:

Commercial Liability	$2,000,000
Blanket Business Personal Property ($500 Deductible)	450,000
Improvements and Betterments ($500 Deductible)	20,000
Business Income with Extra Expense	500,000
Umbrella	1,000,000
EDP Hardware ($250 Deductible)	30,000
EDP Software ($250 Deductible)	3,000
EDP Hardware - Transit ($250 Deductible)	4,000

Miscellaneous Sched. Property ($250 Deductible)	1,000
Commercial Liability ($500 Deductible)	1,000,000
Employee Dishonesty - Blanket ($500 Deductible)	10,000
Forgery & Alteration ($500 Deductible)	10,000
Employee Benefits Liability ($1,000 Deductible)	1,000,000
Stop Gap Liability	1,000,000

Settled claims have not exceeded this commercial coverage in the past three years. The School owns no real estate, but leases a facility located at 425 Jefferson Avenue, Toledo, Ohio. (See Note 17)

B. Workers' Compensation

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

8. 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 administered by the School Employees Retirement Board. SERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to members and beneficiaries. Authority to establish and amend benefits is established by Chapter 3309 of the Ohio Revised Code.

SERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to the School Employees Retirement System, 300 East Broad Street, Suite 100, Columbus, Ohio 43215-3746.

Plan members are required to contribute 9 percent of their annual covered salary and the School is required to contribute an actuarially determined rate. The current rate is 14 percent of annual covered payroll; 5.46 percent was the portion to fund pension obligations for the fiscal year 2002. 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 School's required contribution for pension obligations to SERS for the fiscal years ended June 30, 2002, 2001, and 2000, were $2,712, $3,545, $1,982, respectively; 98.73 percent has been contributed for fiscal year 2002 and 100 percent for fiscal years 2001 and 2000. The unpaid contribution for fiscal year 2002, in the amount of $35 is recorded as a liability.

B. State Teachers Retirement System

The School contributes to the State Teachers Retirement System of Ohio (STRS), a cost-sharing, multiple-employer public employee retirement system administered by the State Teachers Retirement Board. STRS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to members and beneficiaries. Benefits are established by Chapter 3307 of the Ohio Revised Code. STRS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to the State Teachers Retirement System, 275 East Broad Street, Columbus, Ohio 43215-3771.

Plan members are required to contribute 9.3 percent of their annual covered salary and the School is required to contribute 14 percent; 9.5 percent was the portion used to fund pension obligations for the year 2002. Contribution rates are established by STRS, upon recommendation of its consulting actuary, not to exceed statutory maximum rates of 10 percent for members and 14 percent for employers. The School's required contribution for pension obligations to STRS for the fiscal years ended June 30, 2002, 2001, and 2000, were $58,718, $50,944, and $22,875, respectively; 90.09 percent has been contributed for fiscal year 2002 and 100 percent for fiscal years 2001 and 2000. The unpaid contribution for fiscal year 2002, in the amount of $4,908, is recorded as a liability.

9. 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 classified 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 funded on a pay-as-you-go basis.

The State Teachers Retirement 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 shall be included in the employer contribution rate, currently 14 percent of covered payroll. For fiscal year 2002, the Board allocated employer contributions equal to 4.5 percent of covered payroll to the Health Care Reserve Fund. For the School, this amount was $30,139.

STRS pays health care benefits from the Health Care Reserve Fund. The balance in the Fund was $3,256 million at June 30, 2001 (the latest information available). For the fiscal year ended June 30, 2001, net health care costs paid by STRS were $300,772,000, and STRS had 102,132 eligible benefit recipients.

For SERS, coverage is made available to service retirees with ten or more 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.

For the fiscal year ended June 30, 2002, employer contributions to fund health care benefits were 8.54 percent of covered payroll. In addition, SERS levies a surcharge to fund health care benefits equal to 14 percent of the difference between a minimum pay and the member's pay, pro-rated for partial service credit. For fiscal year 2002, the minimum pay has been established at $12,400. For the School, the amount to fund health care benefits, including the surcharge, was $8,070 for fiscal year 2002.

The surcharge, added to the unallocated portion of the 14 percent employer contribution rate, provides for maintenance of the asset target level for the health care fund. The target level for the health care reserve is 150 percent of annual health care expenses. Expenses for health care for the fiscal year ended June 30, 2001 (the latest information available), were $161,439,934, and the target level was $242.2 million. At June 30, 2001, SERS had net assets available for payment of health care benefits of $315.7 million. SERS has approximately 50,000 participants currently receiving health care benefits.

10. OTHER EMPLOYEE BENEFITS

A. Compensated Absences

The criteria for determining vacation are derived from policies and procedures approved by the Governing Board. One member of the management team had vacation leave earned in the year that had not been used at year end. Unused vacation leave is shown as a current liability.

B. Employee Medical, Dental, and Vision Benefits

The School has contracted through the Lucas County Educational Service Center to provide employee medical, dental, and vision insurance to its full-time employees who work 20 or more hours per week. The School pays the full amount of the monthly premiums for the employee for all selected coverage (medical, dental and/or vision). Employees electing the family coverage pay the difference in the premium.

11. STATE SCHOOL FUNDING DECISION

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

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

12. 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 funds. However, in the opinion of management, any such disallowed claims will not have a material adverse effect on the overall financial position of the School at June 30, 2002.

B. Ohio Community School Program

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 law. On April 21, 2003, the Court dismissed the counts containing constitutional claims and stayed the other counts pending appeal of the constitutional issues.

C. School Funding

The Ohio Department of Education conducts reviews of enrollment data 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 results of this review for the fiscal year ended June 30, 2001 resulted in a reduction of $101,693 of state foundation funding. $54,723 was repaid through school foundation deductions for fiscal year 2002 and $46,970, which is included in intergovernmental payables on the face of the financial statements, will be deducted from the School's 2003 monthly foundation payments. The fiscal year 2002 review resulted in no material adjustment.

13. FISCAL AGENT

The School entered into a service agreement with the Treasurer of the Lucas County Educational Service Center to serve as the Chief Financial Officer of the School. As part of this agreement, the School shall compensate the Lucas County Educational Service Center two percent (2%) of the per pupil allotments paid to the School from the State of Ohio (See Note 14). The total contract payment of $18,386 was paid during the year in full.

The Treasurer shall perform all of the following functions while serving as the Chief Fiscal Officer of the School:

A. Maintain custody of all funds received by the School in segregated accounts separate from Lucas County ESC or any other Community School's funds;

B. Maintain all books and accounts of the School;

C. Maintain all financial records of all state funds of the School and follow State Auditor procedures for receiving and expending state funds;

D. Assist the School in meeting all financial reporting requirements established by the Auditor of Ohio;

E. Invest funds of the School in the same manner as the funds of Lucas County ESC are invested, but the Treasurer shall not commingle the funds with any of Lucas County ESC or any other community school; and

F. Pay obligations incurred by the School within a reasonable amount of time, not more than 14 calendar days after receipt of a properly executed voucher signed by the Chief Administrative Officer of the School so long as the proposed expenditure is within the approved budget and funds are available.

14. PURCHASED SERVICE EXPENSES

For the year ended June 30, 2002, purchased service expenses were payments for services rendered by various vendors, as follows:

PURCHASED SERVICES	
Property Services	$165,488
Professional and Technical Services	34,364
Communications	20,760
Meeting Expenses	3,125
Utilities	881
Contracted Craft or Trade Services	9,566
Transportation Services	6,843
LCESC Contracted Services	45,822
Total Purchased Services	$286,849

15. DEBT

Debt outstanding at June 30, 2002, was as follows:

	Outstanding 06/30/01	Additions	Deletions	Outstanding 06/30/02
General Note #1 (Sky Bank)	$200,000		($1,513)	$198,487
General Note #2 (Sky Bank)		$30,000	(134)	29,866
Board Loan (Michael Calabrese)		20,000		20,000
TSFA Parent Organization Loan		6,667	(6,667)	
Lucas County ESC Note #1	4,500		(4,500)	
Lucas County ESC Note #2	7,500		(7,500)	
	$212,000	$56,667	($20,314)	$248,353

The General Note #1 from Sky Bank is a line of credit issued on August 13, 1999, with an amount up to $200,000. The note is secured by the assets of the school. The terms of the note had a maturity date of April 30, 2002. The note was extended for another year and is now payable on April 30, 2003. The interest rate on this line of credit is variable, based on one percent over the prime rate. Total interest expense for the year ended June 30, 2002 was $11,899, of which $938 was payable at year end.

The General Note #2 from Sky Bank is a promissory note issued on February 26, 2002, in the amount of $30,000. The terms of the note had a maturity date of August 26, 2002. The note was extended for another six months and is now payable on February 26, 2003. The interest on this promissory note is 5.75 percent. Total interest expense for the year ended June 30, 2002 was $592, of which $491 was payable at year end.

The board loans in fiscal year 2002 consisted of two $10,000 loans issued from Michael Calabrese, a board member of the School, on July 13 and December 9, 2001 to cover rent expenses for the school year. The amount is payable on demand. Per the agreements, the interest on these promissory notes is 6.00 percent.

Notes are statutorily limited to maturing at the end of the year the note was issued if the debt obligates or is collateralized by the State monies received by the School under Ohio Law. The General Note (Sky Bank), issued during the year, is general in nature and does not specifically exclude State foundation monies and extended beyond year end, contrary to State statutes.

On December 9, 2001, the Parent Organization of the School issued a loan in the amount of $6,667 to cover rent expenses for December. This amount was paid off on February 1, 2002. No interest was assigned to this loan during fiscal year ended 2002.

Lucas County Educational Service Center Note #1 (unsecured) was issued on December 21, 2000, in the amount of $19,500, and matured on June 30, 2001. The School repaid $15,000 during fiscal year 2001, and $4,500 was payable at year end. On August 29, 2001, the entire balance was paid in full. Total interest expense for the year ended June 30, 2002 was $780.

Lucas County Educational Service Center Note #2 (unsecured) was issued on January 26, 2001, in the amount of $7,500, and matured on June 30, 2001. The entire note amount of $7,500 was payable at June 30, 2001. On August 29, 2001, the entire balance was paid in full. Total interest expense for the year ended June 30, 2002 was $300.

16. CAPITALIZED LEASES

The School entered into a capitalized lease for the acquisition of copier equipment. The lease meets the criteria of a capital lease as defined by Statement of Financial Accounting Standards No. 13, "Accounting for Leases," which defines a capital lease generally as one which transfers benefits and risks of ownership to the lessee. The capital lease has been recorded as a fixed asset at the present value of the future minimum lease payments as of the inception date.

The following is a schedule of the future minimum lease payments required under the capital lease and the present value of the minimum lease payments as of June 30, 2002. Payments for principal and interest totaled $7,850 for the fiscal year ending June 30, 2002.

Fiscal Year Ending June 30,	
2003	$7,760
2004	6,612
2005	6,612
2006	551
Total Minimum Lease Payments	21,535
Less: Amount Representing Interest	(1,096)
Present Value of Minimum Lease Payments	$20,439

17. OPERATING LEASE

The School entered into an operating lease for the period August 1, 1999 through July 31, 2003, with Hillenbrand/Zaleski Secor, LLC to lease the third floor of its building for operation of the school facility. In addition, the lease was extended to include a one-year lease of the second floor through June 30, 2002, which was subsequently extended to July 31, 2003. Lease payments totaled $239,335 for the year. At year end, all rent owed to the lessor was paid in full.

The following is a schedule of the future minimum payments required under the operating lease as of June 30, 2002:

Fiscal Year Ending June 30,	
2003	$166,834
2004	13,903
Total Minimum Lease Payments	$180,737

The School has the option to renew the lease for one additional five-year term.

18. MANAGEMENT'S PLANS REGARDING ACCUMULATED DEFICIT (SEE NOTE 3)

The School has an accumulated deficit of $256,833 for the year ended June 30, 2002, and had an operating loss of $370,795. However, the School had net income of $78,336. The School is analyzing operations and admissions procedures to determine appropriate steps to alleviate the deficit and operating loss. Management plans to eliminate the deficit and operating losses with the following actions:

The Board of Directors of the School is still maintaining a working relationship with the external development consultant in efforts to raise more funds to defray the deficit for fiscal year 2002. In addition to hiring a business manager in August of 2002, the Board has also worked extensively to rebuild and strengthen the business office and accounting records systems. This includes monitoring budget to actual information on a monthly basis.

19. RELATED PARTIES

Eric Hillenbrand is part owner of the leasing company (Hillenbrand/Zaleski Development) for the facilities that the School rents and is a board member of the School. Total payments to Hillenbrand/Zaleski Development were $280,254, which includes rent and improvements to the facility.

Board Member Michael Calabrese made two separate loans of $10,000 each to the School in fiscal year 2002 (See Note 15). No payments were made on the loans.

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TOLEDO SCHOOL FOR THE ARTS

SCHEDULE OF FEDERAL AWARDS EXPENDITURES
FOR THE YEAR ENDED JUNE 30, 2002

FEDERAL GRANTOR ***Pass Through Grantor*** Program Title	Pass Through Entity Number	Federal CFDA Number	Receipts	Disbursements
U.S. DEPARTMENT OF EDUCATION				
Passed Through Ohio Department of Education:				
Grants to Local Educational Agencies				
(ESEA Title I)	133942-C1S1-2001	84.010	$18,769	$18,769
	133942-C1S1-2002		1,176	
Total Grants to Local Educational Agencies			19,945	18,769
Special Education Grants to States				
(IDEA Part B)	133942-6BSX-2001-P	84.027	2,795	2,795
Eisenhower Professional Development State Grant				
(Title II)	133942-MSS1-2001	84.281		50
Charter Schools	133942-CHS1-2001-P	84.282	150,000	150,000
	133942-CHS1-2002		150,000	145,883
Total Charter Schools			300,000	295,883
Class Size Reduction				
(Title VI-R)	133942-CRS1-2001	84.340	2,795	4,326
Total Department of Education Federal Expenditures			**$325,535**	**$321,823**

The accompanying notes are an integral part of this schedule.

NOTES TO THE SCHEDULE OF FEDERAL AWARDS EXPENDITURES
FISCAL YEAR ENDED JUNE 30, 2002

NOTE A - SIGNIFICANT ACCOUNTING POLICIES

The accompanying Schedule of Federal Awards Expenditures (the Schedule) summarizes activity of the School's federal award programs. The schedule has been prepared on the cash basis of accounting.

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

Toledo School for the Arts
Lucas County
425 Jefferson Avenue
Toledo, OH 43604-1060

To the Governing Board:

We have audited the financial statements of the Toledo School for the Arts, Lucas County, (the School) for the year ended June 30, 2002, and have issued our report thereon dated May 1, 2003. Our report expressed substantial doubt as to the ability of the School to continue as a going concern. 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 2002-001. We also noted certain immaterial instances of noncompliance that we have reported to management of the School in a separate letter dated May 1, 2003.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the School's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. 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. A reportable condition is described in the accompanying schedule of findings as item 2002-002.

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 consider the reportable condition described above to be a material weakness. 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 May 1, 2003.

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

Betty Montgomery

Betty Montgomery
Auditor of State

May 1, 2003

Auditor of State
Betty Montgomery

INDEPENDENT ACCOUNTANTS' REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO MAJOR FEDERAL PROGRAMS AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH *OMB CIRCULAR A-133*

Toledo School for the Arts
Lucas County
425 Jefferson Avenue
Toledo, OH 43604-1060

To the Governing Board:

Compliance

We have audited the compliance of the Toledo School for the Arts, Lucas County, (the School) with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133, Compliance Supplement* that are applicable to its major federal program for the year ended June 30, 2002. The School's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings. Compliance with the requirements of laws, regulations, contracts and grants applicable to its major federal program is the responsibility of the School's management. Our responsibility is to express an opinion on the School's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance occurred with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program. An audit includes examining, on a test basis, evidence about the School's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the School's compliance with those requirements.

In our opinion, the School complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended June 30, 2002. We noted an instance of noncompliance that does not require inclusion in this report that we have reported to the management of the School in a separate letter dated May 1, 2003.

One Government Center / Room 1420 / Toledo, OH 43604-2246
Telephone: (419) 245-2811 (800) 443-9276 Fax: (419) 245-2484
www.auditor.state.oh.us

Internal Control over Compliance

The management of the School is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the School's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. 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 noncompliance with applicable requirements of laws, regulations, contracts and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses. We noted a matter involving the internal control over federal compliance that does not require inclusion in this report, that we have reported to management of the School in a separate letter dated May 1, 2003.

This report is intended for the information and use of the audit committee, management, the Governing Board, the Sponsor, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Betty Montgomery

Betty Montgomery
Auditor of State

May 1, 2003

TOLEDO SCHOOL FOR THE ARTS

SCHEDULE OF FINDINGS
OMB CIRCULAR A -133 § .505
FOR THE YEAR ENDED JUNE 30, 2002

1. SUMMARY OF AUDITOR'S RESULTS

(d)(1)(i)	**Type of Financial Statement Opinion**	Unqualified
(d)(1)(ii)	**Were there any material control weakness conditions reported at the financial statement level (GAGAS)?**	Yes
(d)(1)(ii)	**Were there any other reportable control weakness conditions reported at the financial statement level (GAGAS)?**	No
(d)(1)(iii)	**Was there any reported material noncompliance at the financial statement level (GAGAS)?**	Yes
(d)(1)(iv)	**Were there any material internal control weakness conditions reported for major federal programs?**	No
(d)(1)(iv)	**Were there any other reportable internal control weakness conditions reported for major federal programs?**	No
(d)(1)(v)	**Type of Major Programs' Compliance Opinion**	Unqualified
(d)(1)(vi)	**Are there any reportable findings under §.510?**	No
(d)(1)(vii)	**Major Programs (list):**	Charter School CFDA # 84.282
(d)(1)(viii)	**Dollar Threshold: Type A\B Programs**	Type A: > $ 300,000 Type B: all others
(d)(1)(ix)	**Low Risk Auditee?**	No

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

FINDING NUMBER 2002-001

Noncompliance Citation

Community schools may issue debt. However, if the debt obligates or is secured by State monies received by the community school under Ohio Revised Code §3314.08(D), then the debt must be issued in accordance with Ohio Revised Code § 3314.08(J), which states, in part, that "the school may issue notes to evidence such borrowing to mature no later than the end of the year in which such money was borrowed."

FINDING NUMBER 2002-001
(Continued)

During the year ended June 30, 2002, the School issued three notes in the amounts of $30,000, $10,000, and $10,000 and also received a loan extension on the $200,000 note from the prior year, with all notes having a maturity date that extends beyond the fiscal year end of June 30, 2002. The notes in question are general in nature. Because the notes do not specifically exclude the School's Ohio Revised Code § 3314.08(D) funds from the general collateral provisions, these notes obligate these monies. Therefore, Ohio Revised Code §3314.08(J) applies.

We recommend the School take steps to monitor debt and determine/ensure there is no outstanding debt subject to Ohio Revised Code § 3314.08(J) at year end.

FINDING NUMBER 2002-002

Material Weakness - Purchasing

Forty percent of the purchase orders tested did not have the Fiscal Agent's signature approving the purchase.

Review and approval of expenditures by the Fiscal Agent is a key control in the disbursement process to determine that expenditures are for a proper purpose, within budget, and charged against proper fund code.

Lack of proper review and approval could result in funds being spent on purchases that are not for a proper public purpose, disbursements that exceed the budgeted amount, payments being made to fictitious vendors and expenditures not being charged to the correct account.

We recommend the Fiscal Agent review and sign every purchase order before a check is paid to a vendor.

3. FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS

None.

TOLEDO SCHOOL FOR THE ARTS

SCHEDULE OF PRIOR AUDIT FINDINGS
JUNE 30, 2002

Finding Number	Finding Summary	Fully Corrected?	Not Corrected, Partially Corrected; Significantly Different Corrective Action Taken; or Finding No Longer Valid; ***Explain***:
2001-10148-001	ORC § 3314.08(J) debt maturity date extends beyond end of the year.	No	Not corrected. Reissued as Finding Number 2002-001.
2001-10148-002	Fiscal Agent Agreement – debt obligations not paid when due.	Yes	Finding No Longer Valid.
2001-10148-003	Ohio Revised Code § 3314.03(A)(10) qualification of teachers.	No	Partially corrected. Reported as management letter comment.
2001-10148-004	Weak controls over fixed assets.	No	Partially corrected. Reported as management letter comment.

Auditor of State
Betty Montgomery

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TOLEDO SCHOOL FOR THE ARTS

LUCAS 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
JUNE 17, 2003